*Volume 39, No. 1, April 25, 2025*

# QUARTERLY UPDATE

## CWS CAPITAL PARTNERS LLC

*CWS Capital Partners LLC*

CWS

### CALENDAR OF EVENTS

**May 26, 2025**
Memorial Day Holiday
CWS Offices Closed

**June 16, 2025**
2nd Quarter 2025
Estimated Tax Payments Due

**July 4, 2025**
Independence Day Holiday
CWS Offices Closed

**July 25, 2025**
2nd Quarter 2025
Quarterly Reports & Distributions

**September 1, 2025**
Labor Day Holiday
CWS Offices Closed

**September 15, 2025**
3rd Quarter 2025
Estimated Tax Payments Due

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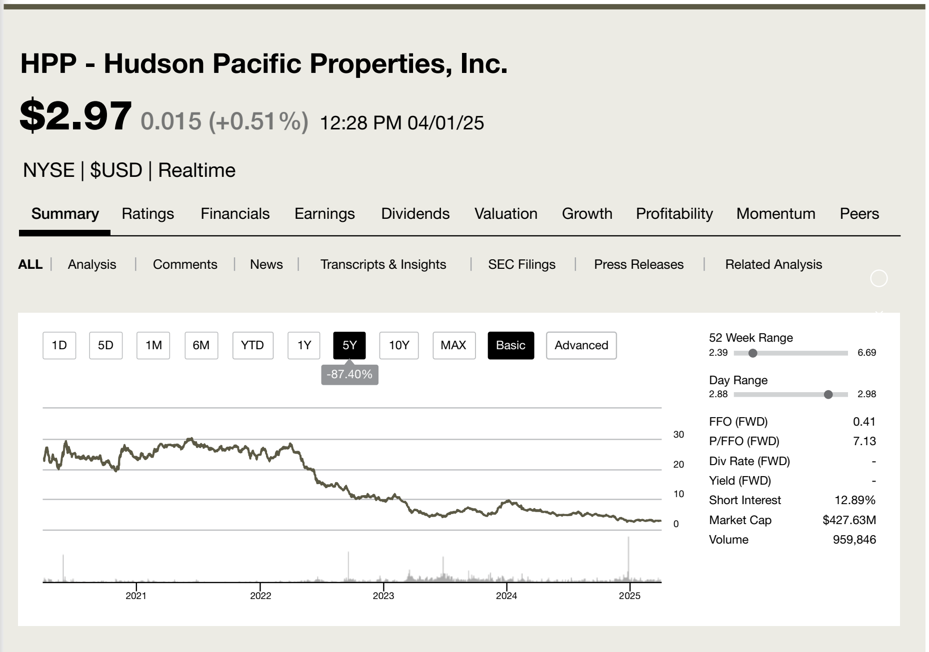
# TURNING THE CORNER

*By Gary Carmell*

This article is based on my presentation that I made at our Annual Partners Meeting that took place on April 8th.

Let me first start off by saying that I'm glad we don't focus on the office market. Here is a chart of Hudson Pacific Properties. Long-term shareholders have seen the value of their investment decimated.

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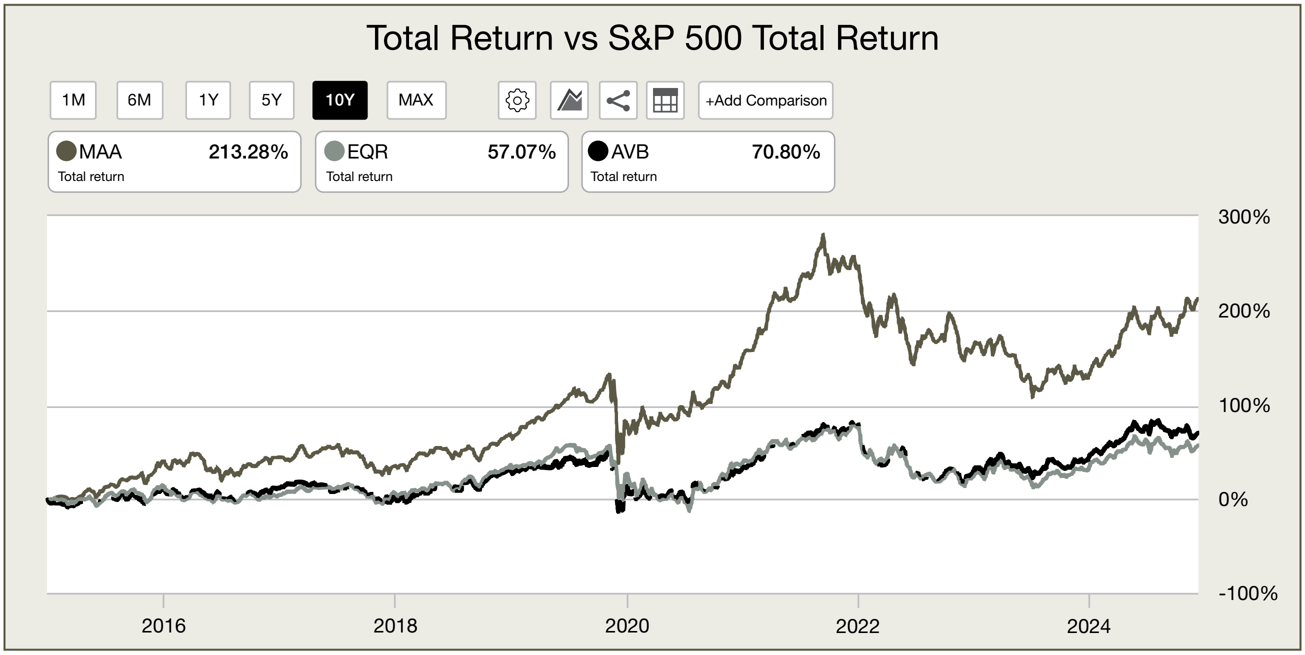
And even for apartment owners, in which long-term value has held up, market selection has been critically important as this chart comparing Mid-America Apartment Communities (MAA), which is more similar to CWS with its Sunbelt and suburban emphasis, and Equity Residential and AvalonBay, which are more coastal and urban focused, shows.




As an aside, both EQR and AvalonBay are now making a push to diversify into non-coastal markets now.

If we drill down more deeply into MAA's performance, we can see from the following table that over five and 10 years shareholders have done quite well. The last three years, and more specifically, the first two of those years were terrible as bubble-type valuations deflated. The one-year return shows that we are now in a recovery, thawing phase.

**Price Performance**

| | 1w | 1M | 6M | YTD | 1Y | 3Y | 5Y | 10Y |
|---|---|---|---|---|---|---|---|---|
| **Price Return** | 1.75% | -0.92% | 4.83% | 7.76% | 26.59% | -20.47% | 61.67% | 115.57% |
| **S&P 500** | -2.52% | -5.57% | -2.43% | -4.41% | 7.01% | 24.11% | 117.54% | 171.89% |
| **Total Return** | 1.75% | -0.92% | 6.91% | 8.85% | 31.94% | -11.09% | 91.36% | 204.95% |
| **S&P 500 Total Return** | -2.50% | -5.45% | -1.78% | -4.09% | 8.46% | 29.98% | 135.03% | 225.44% |

This very much mirrors CWS' experience. The long-term has been rewarding but our performance has been negatively impacted by the dramatic increase in interest rates, particularly short-term rates, from mid-2022 through August 2024 as this chart shows.*

*Past performance is not indicative of future results.

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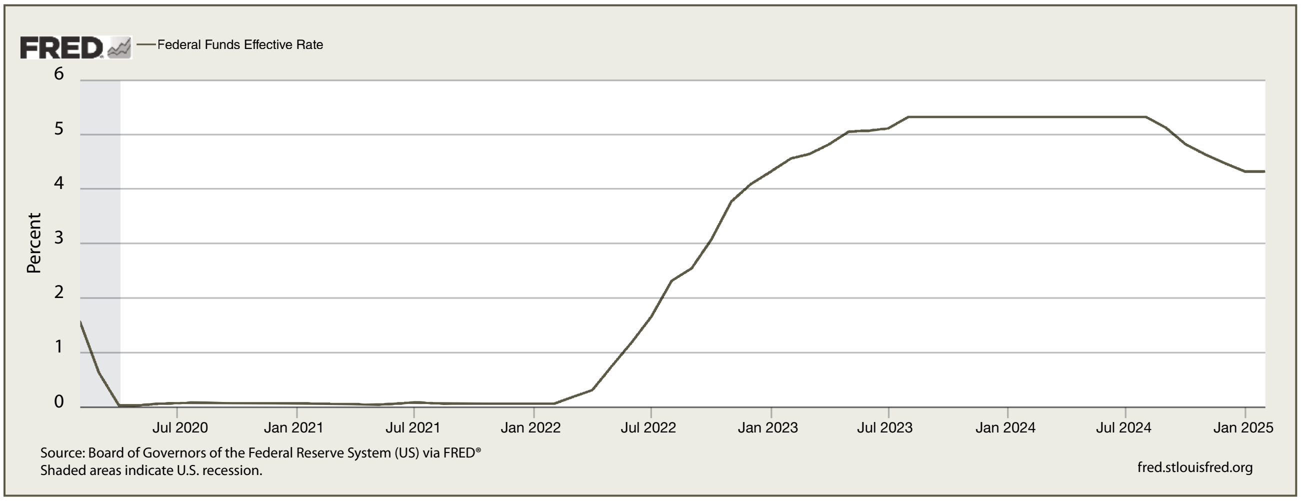


The rapid rise in interest rates resulted in borrowing costs going up quite significantly. This led to buyers unwilling to pay the same prices that were clearing the market in 2021 and early 2022. Sellers kept looking through the rearview mirror and most were unwilling to lower their prices which created a big gap between buyers and sellers. As a result, transaction volume dropped dramatically.

During this freezing period we had to go on defense, particularly for our 2021-2022 acquisitions that were purchased towards the top of the market when rates were much lower, and for some of our urban properties that were dealing with the fallout of Covid, remote work, crime, and renter fraud, pro-tenant legislation, longer eviction periods, etc.

Of our 106 properties, nine were purchased in the 2021-22 period when values were quite elevated. And while of course we would have preferred to not be buying during this time frame, we were also carrying out 1031 exchanges so we didn't have a choice if we wanted to complete the exchanges and defer the taxes. Fortunately, as a percentage of the CWS portfolio these represent a relatively small percentage.

Because our financing was largely floating-rate, the rapid rise in interest rates necessitated we bring in capital for more properties than the 2021-22 vintage. To date we have had to bring in capital for 21 properties (approximately 20% of the portfolio) since 2023. As a percentage of portfolio equity, however, the additional capital is relatively small as it has been approximately $38.7 million out of an estimated $3 billion of equity. This represents approximately 1.3% of the market value of investor equity. Of course, each investment will be significantly higher because almost 80% of properties have not required additional capital. For investors who have been asked to fund capital calls, their pro rata share has, on average, equaled approximately 2.7% of the value of the market value of their equity.

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I would categorize the additional capital needs as follows:

| 2021-22 Vintage | Urban/Atlanta | Development | Other |
|---|---|---|---|
| 6 | 9 | 2 | 4 |
| Dominion | Marq 211 | The Bennett | Rim |
| Nash | Buckhead | The Gabriel | TPC |
| Iliff Station | Midtown District | | Parkside |
| Promenade | Ponce | | Westchase |
| Chandler | Skyline West | | |
| Brunswick | Marq 31 | | |
| | WaterMarq | | |
| | Anthem | | |
| | SoCo on the Lake | | |

With interest rates having dropped and the cost of interest rate caps falling dramatically, our properties with floating-rate loans are healthier from a cash flow standpoint, although not all are out of the woods yet, but the trend could be our friend here as I will discuss later.

We have had a number of loans maturing as well as some that we refinanced prior to their maturity date over the past year. In general, these have been positive for our investors. Between January 2024 and April 30, 2025, we will have refinanced 18 properties representing over $550 million in debt. Of these, there were 16 fixed-rate and two floating-rate. We will have distributed approximately $64.4 million to our investors, which fortunately is more than we have requested in terms of capital calls.

The two floating-rate loans required higher leverage that could only be accessed from debt funds that only offer floating-rate loans, given they in turn borrow using floating-rate debt. Thus, for the 16 others in which we had discretion to choose between floating and fixed, we chose fixed for all of them. This is a radical departure from our heavy reliance on floating-rate debt between 2011 and 2022.

I think the following tables show why the game has changed. The first one is the comparison between floating and fixed between 1/1/2011 and 4/30/2022. The second table reflects rates currently. One can see that floaters were far cheaper and offered much better prepayment flexibility.

| | Fixed | Floating |
|---|---|---|
| Index* | 2.11% | 0.50% |
| Spread | 1.75% | 1.67% |
| Average Rate | 3.86% | 2.17% |

*The index for Fixed is the 7-year Treasury yield while for floating it's the 30-day T-Bill yield which is a proxy for 30-day Libor which has been discontinued.

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| | Fixed | Floating |
|---|---|---|
| Index* | 3.85% | 4.33% |
| Spread | 1.25% | 1.95% |
| Average Rate | 5.10% | 6.28% |

*The index for Fixed is the 7-year Treasury yield while for floating it's the 30-day SOFR..

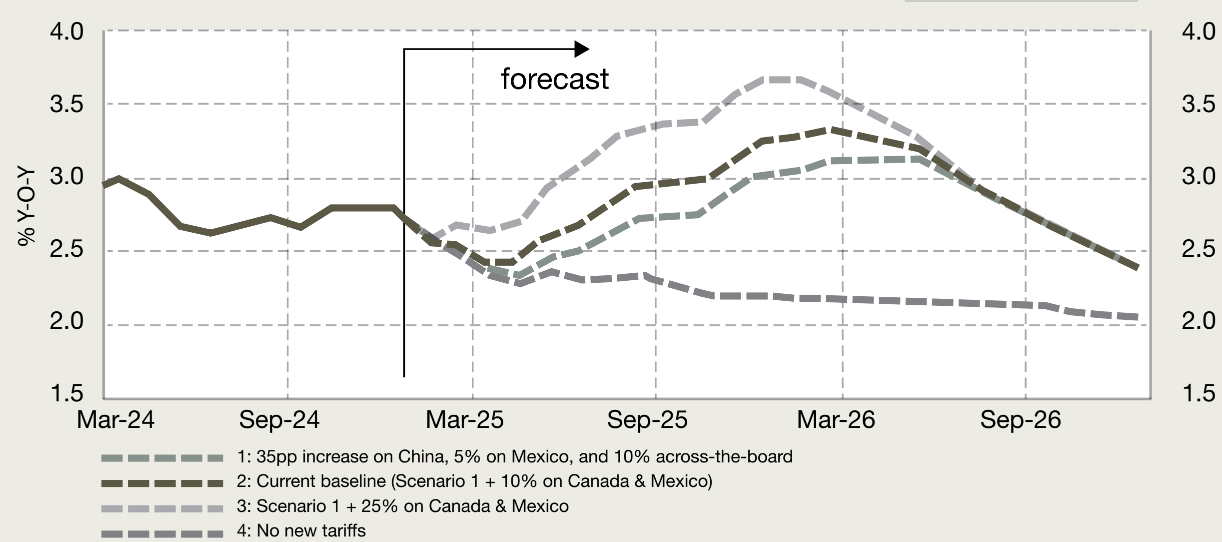
One can see that today fixed rates are quite a bit lower than floaters. This is because the spreads have compressed quite a bit for fixed-rate loans and widened for floaters. In addition, the index is lower for the fixed-rate loan as compared to a floating-rate loan. The Fed needs to cut by almost 1% to have floaters come down to match fixed-rate loans. The cost of floating-rate loans should also include the price of purchasing and maintaining interest rate caps, which are not reflected in these calculations.

And while the drop in Treasury yields suggests that the Fed will need to restart rate cuts with the economy projected to weaken quite materially, and even contract during the first quarter, the prospect of tariffs makes the Fed's inflation fight even more difficult, which creates a wider band of uncertainty for variable-rate borrowers.

**Bob Elliott**
@BobEUnlimited

The Fed is understandably cautious about the possible impact of tariffs ahead.

**Fig. 8: Tariffs are likely to push up inflation in the medium term** Core PCE inflation




**Bob Elliott**
@BobEUnlimited
Mar 12

There are signs that inflation is starting to perk up again as the new admin policies are digested thru the economy.
Businesses are indicating a desire to raise prices and consumers expect higher inflation ahead even as backward looking measured inflation moderates....

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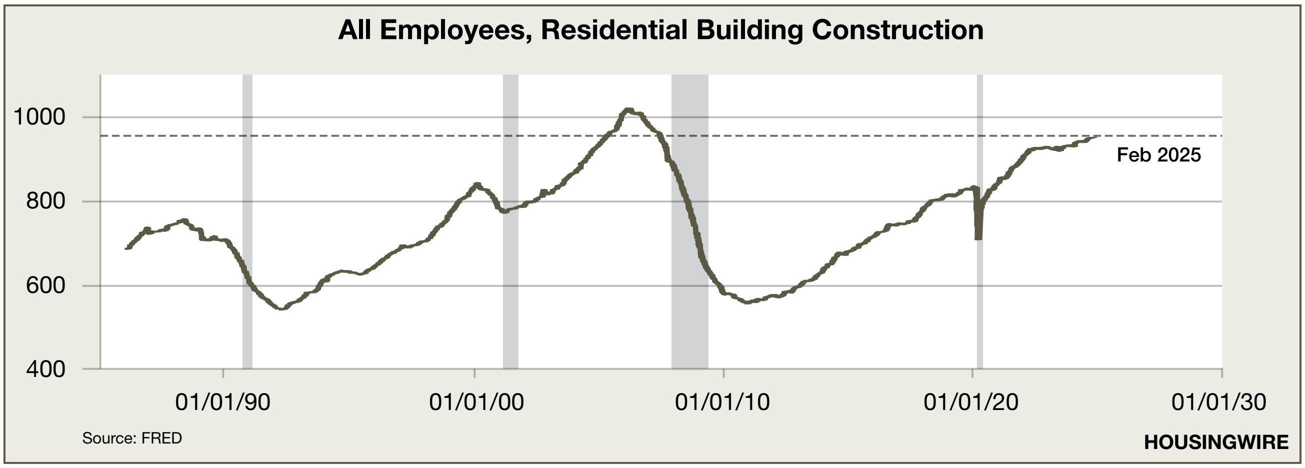
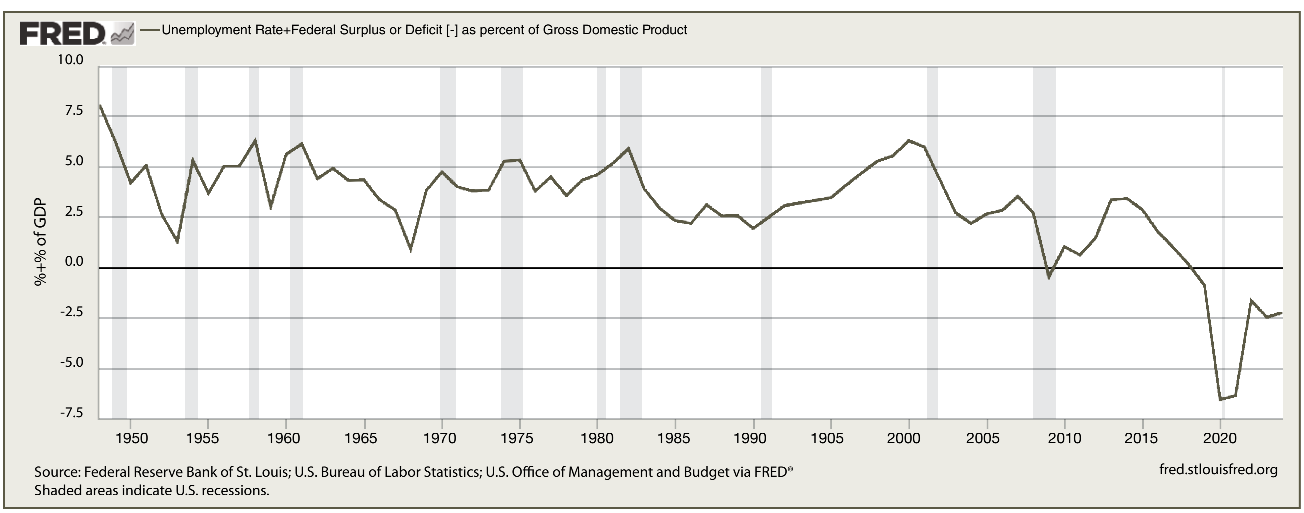
After the most recent refinances, including those closing at the end of April, approximately 1/3 of our portfolio will be fixed rate. There are a few other loans we are considering refinancing into fixed so this percentage will probably increase. At the same time, we are also well positioned to benefit from the potential of the Fed cutting rates below 3.50% in the event of a recession.

Right now the economy has held up far better than most people expected given how fast rates went up and how high they went. In my opinion, the principal reason for this is the incredible strength of the construction employment market and extraordinary government spending. Normally we would have seen approximately one million construction jobs lost based on higher rates and past downturns. As this chart shows, not only have jobs not been lost in the construction sector, but they have actually grown.




In addition, the federal deficit, which is typically about 3% less than the unemployment rate, has been running 2.5% GREATER than the unemployment rate, which is providing extraordinary stimulus to the economy. This has been helping the economy immensely.

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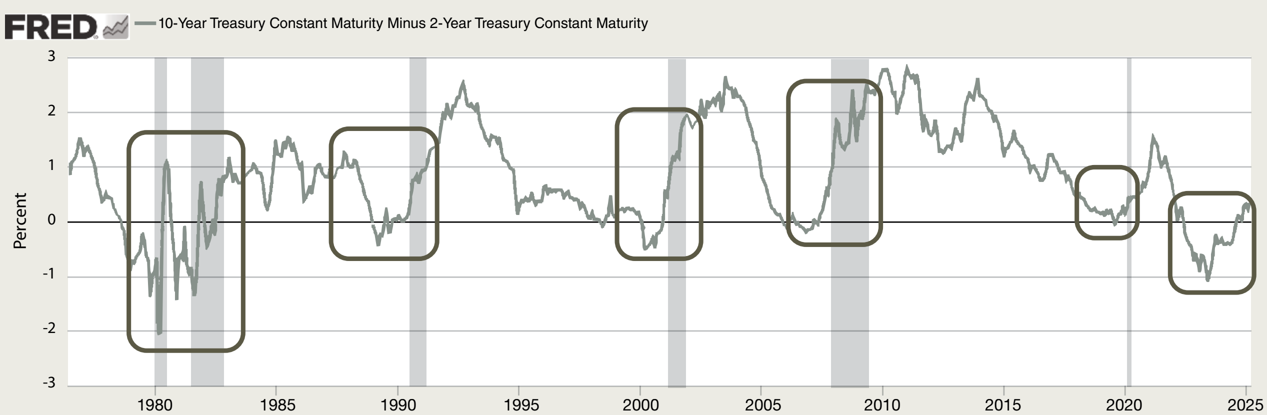
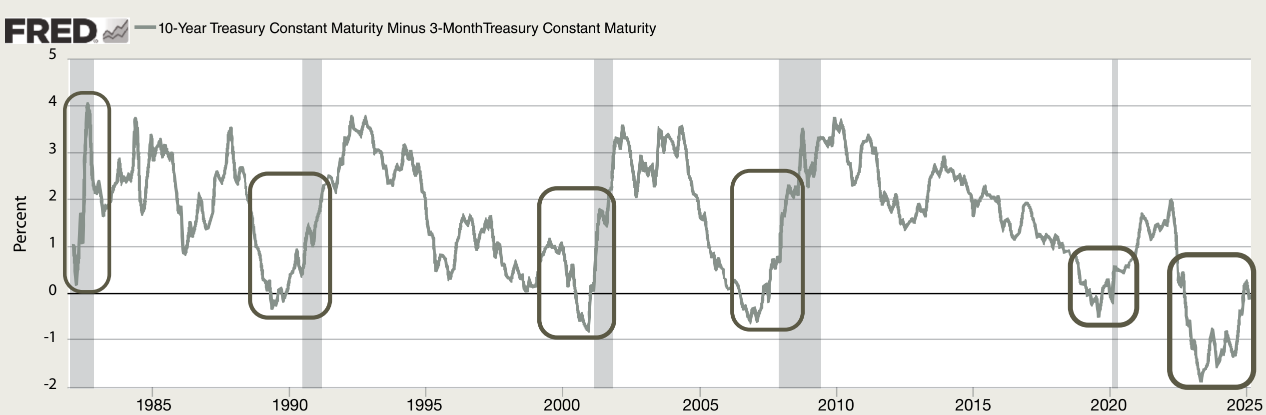
With DOGE and tariffs, however, there is very much risk that the economy is going to weaken. In fact, markets are already factoring this in with the big drop in Treasury yields and huge downturn in the stock market.

If the yield curve is an indication of future economic activity, the signs are looking a bit ominous. As I have written about quite a bit over the last year, especially in my weekly blog, recessions don't start when the yield curve inverts, this is when short rates are higher than long rates, but when the curve de-inverts and long rates return to being higher than short rates. As these charts show, we are now at this point so the clock has definitely started to be on recession watch.

## Is This Time Really Different? Why?




Source: Federal Reserve Bank of St. Louis via FRED®
Shaded areas indicate U.S. recession.
fred.stlouisfred.org




Source: Federal Reserve Bank of St. Louis via FRED®
Shaded areas indicate U.S. recession.
fred.stlouisfred.org

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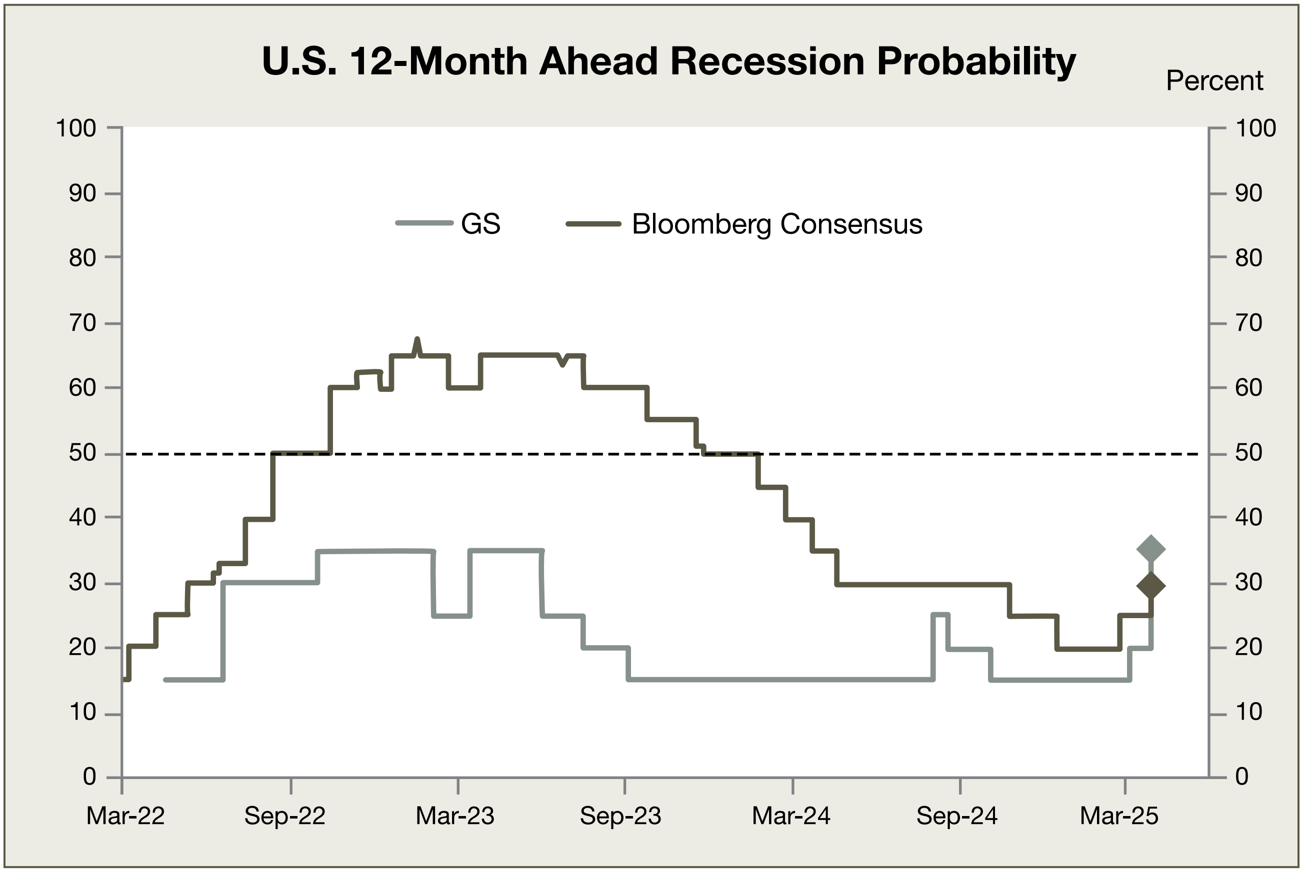
Goldman Sachs has been more bullish than the consensus of Wall Street economists in terms of the economy staying out of a recession. And while it still puts the percentage at less than 50%, it is now slightly more bearish than the consensus for the first time in three years.




From a CWS perspective, we are intensely focused on having those subset of properties in our portfolio that are still generating negative cash flow to turn the corner to reach breakeven. I think of these as our triage properties. Their Net Operating Income (NOI) is not only still too low to reach breakeven based on current interest rates, as almost all of these have floating rate loans, but they also cannot be refinanced until their Net Operating Incomes grow substantially.

And while on the surface this may sound concerning, there is hope as these properties will benefit quite materially if the Fed finds that it has to lower rates below the 3.00% to 3.50% floor being priced in by the market. A number of these properties should hit break even or turn positive if the Fed cuts rates to 3.00% without factoring in growth in NOI.

And while an economic slowdown can be challenging for apartment performance as demand may be reduced due to a lack of jobs impacting household formations, apartment rents are also a bargain as compared to the cost of purchasing and owning a home as well as the rents required to justify building as this chart shows.

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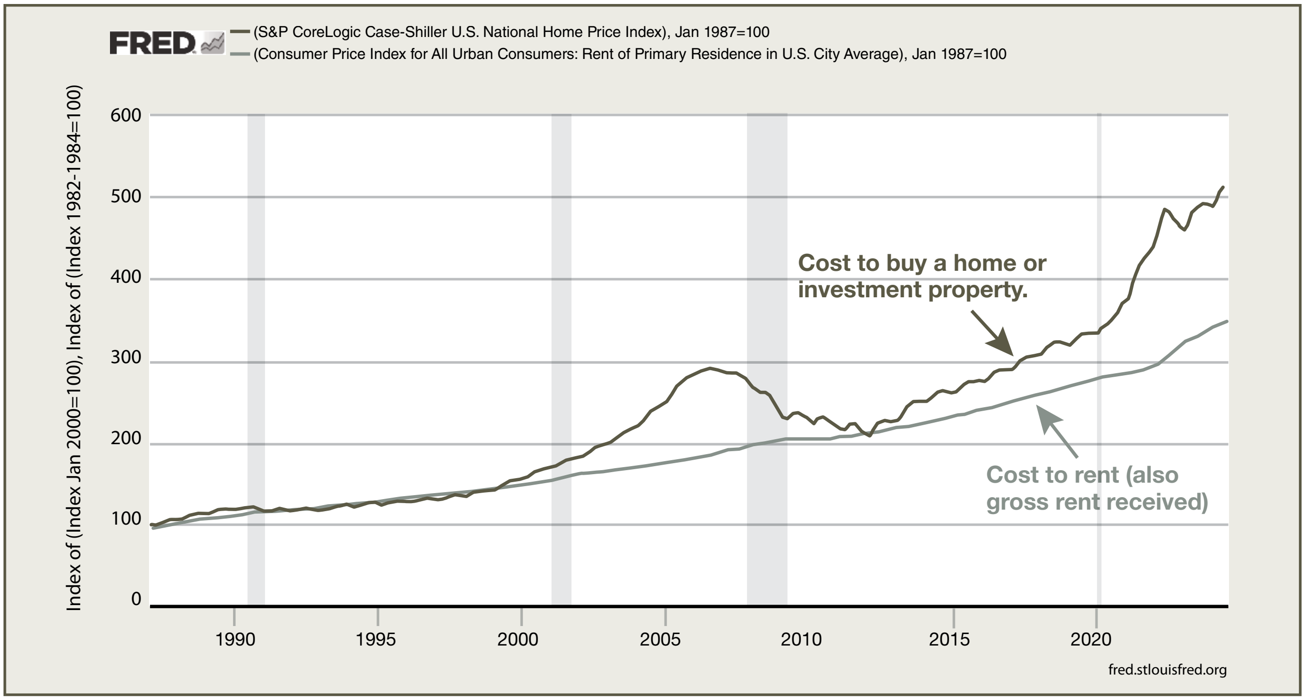


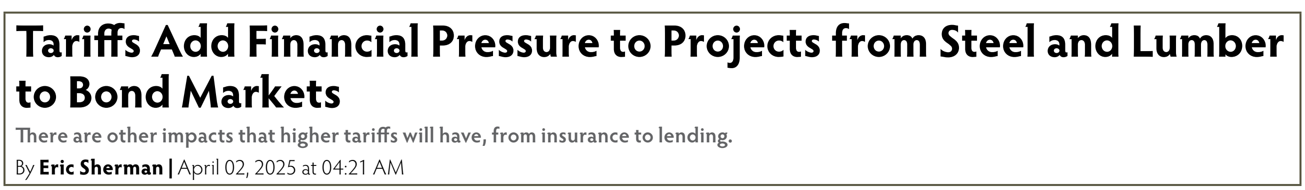

In addition, if tariffs ripple through to the cost of construction materials, as these headlines suggest may already be happening, then rents need to go even higher before they are at a level to justify building new apartment communities.


INSIDE WEALTH

**Tariff fears are raising construction costs by up to 20%, says Related Group CEO**

PUBLISHED FRI. MAR 21 2025·11:16 AM EDT

By **Robert Frank** @ROBTFRANK


**Tariffs Add Financial Pressure to Projects from Steel and Lumber to Bond Markets**

There are other impacts that higher tariffs will have, from insurance to lending.

By **Eric Sherman |** April 02, 2025 at 04:21 AM

With more cash going out to our investors than cash needed to support our more challenged properties, and interest rates dropping, it does feel like we're turning the corner. We still have other properties that could be compelling candidates for refinances, many others that will benefit from the Fed cutting rates, and a portfolio of properties in dynamic, growing markets, in which the rents can grow quite substantially before they are high enough to stimulate another wave of building, particularly with costs rising due to the impact of tariffs.



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