# KKR Real Estate Trust

## Q2 2023 Earnings Call

## July 25, 2023, at 10:00 a.m. Eastern

**CORPORATE PARTICIPANTS**

**Jack Switala** – *Investor Relations*

**Matt Salem** – *Chief Executive Officer*

**Patrick Mattson** – *President and Chief Operating Officer*

**Kendra Decious** – *Chief Financial Officer*

## PRESENTATION

**Operator**
Good morning, and welcome to the KKR Real Estate Finance Trust Inc. Second Quarter 2023 Financial Results Conference Call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star then one on your touchtone phone. To withdraw your question, please press star then two. Please note, this event is being recorded.

I would now like to turn the conference over to Jack Switala. Please go ahead.

**Jack Switala**
Great. Thanks, operator, and welcome to the KKR Real Estate Finance Trust Earnings call for the second quarter of 2023. As the operator mentioned, this is Jack Switala. Today, I'm joined on the call by our CEO, Matt Salem; our President and COO, Patrick Mattson; and our CFO, Kendra Decious.

I'd like to remind everyone that we will refer to certain non-GAAP financial measures on the call, which are reconciled to GAAP figures in our earnings release and in the supplementary presentation, both of which are available on the Investor Relations portion of our website. This call will also contain certain forward-looking statements which do not guarantee future events or performance. Please refer to our most recently filed 10-Q for cautionary factors related to these statements.

Before I turn the call over to Matt, I'll provide a brief recap of our results. For the second quarter of 2023, we reported a GAAP net loss of $25.8 million or negative $0.37 per diluted share, including a CECL provision of $56.3 million or $0.82 per diluted share. Distributable earnings this quarter were $33.1 million or $0.48 per share.

Book value per share as of June 30, 2023, was $16.38, a decline of 4.5% quarter-over-quarter. Our CECL allowance increased to $3.30 per share from $2.48 per share last quarter. The increase was primarily due to additional reserves on risk-rated 5 senior office loans as well as macroeconomic conditions.

Finally, in June, we paid a cash dividend of $0.43 per common share with respect to the second quarter. Based on yesterday's closing price, the dividend reflects an annualized yield of 13.5%.

With that, I'd now like to turn the call over to Matt.

**Matt Salem**
Thanks, Jack. Good morning and thank you for joining us today. KREF generated another quarter of strong distributable earnings of $0.48 per share relative to our $0.43 per share dividend. Distributable earnings continue to benefit from the higher interest rate environment. While higher interest rates are beneficial from an earnings standpoint, this dynamic has created challenges for commercial real estate with little capital markets liquidity and declining asset valuations.

We anticipate the current dislocation and associated volatility will persist for the foreseeable future. Regional banks have begun pulling back from the market while larger money center banks remain cautious. Borrowers will need to recapitalize, take equity infusions or sell assets as approximately $1 trillion of commercial real estate loans mature in 2023 and 2024.

Notably, the CRE lending market is highly competitive for stabilized in-favor assets with insurance capital very active. This environment warrants patience and discipline, with a particular focus on liabilities with duration and durability, considerations we have had front of mind in building KREF.

Despite the volatility, we have seen progress on a number of initiatives. First, we're in the late stages of a sales process on our risk-rated 5 Philadelphia loan. Second, our borrowers are marketing a risk-rated 4 D.C. office asset with initial indications above our $162 million loan amount after significant progress on the business plan. The property is near stabilization having signed over 70,000 square feet of leases year-to-date with total occupancy increasing from the low 60s to the high 80s. Third, many of our other office sponsors are signing leases. Excluding the leases, I just mentioned, our office assets have signed over 435,000 square feet of leasing year-to-date, including the largest lease in Philadelphia in 18 months. Finally, subsequent to quarter end, our Oakland, California office loan was paid down by 68% in connection with the lease modification and PACE financing, and we expect full repayment in the summer of 2024.

KREF's steady focus on building non-mark-to-market financing sources and maintaining high levels of liquidity over the past few years has proved crucial in navigating this kind of environment. We continue to have ample liquidity, ending the quarter with $800 million of availability, including $208 million of cash and $560 million of corporate revolver capacity. We had no new loan originations this quarter as we focused on maintaining a robust liquidity position.

At quarter end, nearly 70% of our portfolio was comprised of multifamily, industrial and risk-rated 3 office property types. The multifamily portion of our portfolio continues to perform well with weighted average rent increases of 7.5% year-over-year.

In the second quarter, loan repayments totaled $339 million, creating a net portfolio reduction of $162 million. With floating rate coupons at mid-8% today versus takeout financing closer to 6% for stabilized properties, we are beginning to see borrowers opt for fixed rate refinancings. Beyond KREF, KKR is actively lending across a diverse CRE capital base, including bank and insurance SMAs and private debt funds, which allows us to stay active in the market and service our strong client relationships.

Our integration with KKR's broader real estate business that manages $65 billion of assets provides us with real-time market knowledge across both debt and equity. Our team of approximately 150 professionals has a strong reputation as a best-in-class capital solutions provider. We also continue to benefit from our longstanding banking relationships as part of the broader KKR franchise. As we have previously stated, we expect the portfolio to turn over modestly in 2023 and anticipate future funding should be offset by future repayments for the full year.

A lack of capital market liquidity continues to challenge the office sector. We increased reserves this quarter, primarily driven by a higher reserve on an existing watch list loan that was downgraded to a risk rating of 5 in the quarter. At this point, we believe we have identified all the potential office issues in our watch list and do not anticipate further ratings migration within the 3-rated office loans. While we are focused on long-term solutions to resolve watch list loans, we are seeking to maximize shareholder value, and where there is a dearth of liquidity, we have tools at our disposal to seek other options, including modifying loans, taking title, and managing properties. I expect we'll have various outcomes as we work through the 5-rated loans.

KREF was built for moments like this. We are operating KREF with $800 million of liquidity. 76% of our secured financing as of quarter end was fully non-mark-to-market. We upsized a master repurchase agreement from $240 million to $400 million, all while succeeding and terming out our debt with KREF

having no corporate debt or final facility maturities due until late 2025. And we have a robust real estate business with a strong reputation across real estate equity, debt and asset management.

Finally, it is worth mentioning our manager's ownership of approximately 14% of KREF's shares outstanding today, which we believe is the highest percentage held by a manager in the mortgage REIT sector and demonstrates meaningful alignment between KKR and KREF.

With that, I'll turn the call over to Patrick.

**Patrick Mattson**
Thank you, Matt. Good morning, everyone. I'll begin by providing a CECL reserve and watch list update, followed by our efforts on the capital and liquidity front.

This quarter, we recorded a $56 million increase in our CECL reserve for a total reserve of $228 million or 304 basis points of our loan principal balance. This increase in our reserve was due mainly to additional reserves taken on our office loans risk-rated 5, most notably with the addition of the Mountain View, California office loan that had a principal balance of $200 million at June 30.

Approximately two-thirds of our total CECL reserve is held against our three 5-rated loans. The Mountain View office loan was initially placed on the watch list in third quarter 2022. The properties are recently renovated, very high-quality Class A office campus but is located in a more challenged leasing market. And we transitioned the asset to nonaccrual status in June. At this time, we are considering next steps for the asset, which may include taking ownership as we work with the sponsor on a transition plan. As we have noted in prior quarters, when loans move from a four to five risk rating, there's generally a meaningful increase in our loss expectation.

Regarding our $194 million Minneapolis office, we have decided to modify the loan after testing the sales market. The loan was restructured this quarter with a two-year term and bifurcated into a $120 million fully funded senior mortgage loan and a $79 million mezzanine note, including $5 million of proceeds for future leasing. The senior loan is current on contractual interest payments through July.

This property is well positioned to capture tenant demand as it's one of the best buildings in the market in terms of both quality and location and has leased over 100,000 square feet over the last 18 months. The renovated Class A property is nearly 80% leased with adequate cash flow to cover the senior debt service. And as tenants seek space in well-capitalized buildings that can offer attractive leasing packages, we expect further positive momentum. The loan extension ensures the building is capitalized to fund leasing costs as we feel this approach preserves optionality to optimize the value of the asset for KREF.

On the risk-rated 5 Philadelphia office loan, we are working with the existing sponsor on a short sale process in which we will provide financing to a new equity sponsor. If the sale occurs, we'll recognize a loss through our cash metric of distributable earnings.

We added one Boston office loan to the watch list this quarter, which is secured by a Class A office located in downtown Boston on Cambridge Street. The property is currently 90% leased. Though given our conservative approach to identifying assets of concern, we downgraded this loan, given the elevated loan-to-value ahead of the loan's initial maturity in first quarter 2024.

Away from the watch list our risk-rated 3 office portfolio, which equates to just under half of the outstanding principal balance of the office segment, continues to perform well and has attractive credit metrics. In aggregate, the seven properties representing these underlying risk-rated 3 office properties

are 93% leased with a weighted average debt yield of 8.9% and a median 8.4 years of weighted average lease term remaining. Importantly, as Matt mentioned earlier, we don't foresee any negative ratings migration on our remaining 3-rated office loans.

The average risk rating of the portfolio was 3.2, consistent with the prior quarter and 83% of our portfolio is risk-rated 3 or better. Our portfolio is 99% floating rate. And in the second quarter, we completed our transition to SOFR, and now all our floating rate assets and liabilities are benchmarked to the market convention rate.

One of KREF's key differentiators is the composition of its financing structure. 76% of our outstanding financing remains fully non-mark-to-market, and the remaining balance is marked to credit only. We continue to optimize and in the second quarter, we upsized a $240 million master repurchase agreement to $400 million. Excluding match term secured financing, there are no corporate debt or final facility maturities until fourth quarter 2025.

KREF is well capitalized with a debt-to-equity ratio of 2.2x and total look-through leverage ratio of 4.0x as of quarter end. As of June 30, KREF had $208 million of cash and $560 million of corporate revolver capacity available. The resiliency of our financing structure, coupled with our independence from the public capital markets, buffers KREF on the liability side during times of capital markets volatility.

Thank you for joining us today. Now we're happy to take your questions.

**QUESTIONS AND ANSWERS**

**Operator**
We will now begin the question-and-answer session. To ask a question, you may press star then one on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you would like to withdraw your question, please press star then two. At this time, we will pause momentarily to assemble our roster.

The first question today comes from Rick Shane with JPMorgan.

**Rick Shane**
Hey guys, thanks for taking my question. The one disadvantage of being first is I'm still kind of pulling some data for the background on this question, so if I trip some things up, I apologize. I'd like to talk a little bit about the Minneapolis transaction. Obviously, you cut the spread on the deal on the floating rate portion by about 150 bps. The PIK component on the mezz, and this is, I think, the thing that surprises me, is fixed rate and it's actually below the coupon on the senior. So, I guess a couple of things. Did the sponsor put in additional equity? And to the extent this deal was restructured and extended, where is the upside for you? What is the optionality that if this is presumably sort of buy the sponsor additional time in order to sell the property, where do you guys participate in the benefit of that transaction?

**Patrick Mattson**
Good morning, Rick. I'll take the question. It's Patrick.

So to answer specifically, no, there was no additional sponsor equity into this deal. As we've said and as you know, this is a cash flowing asset. So, one of the benefits that we have here is that we've got an asset that is nearly 80% leased, it's got cash flow that can support debt service, and the structuring really allowed us to play the asset forward here, continue to finance it at an attractive basis. It gives

clearly the sponsor some optionality here, but also gives us optionality to not sell into what's obviously not a great capital markets environment, so we're able to play it forward and look for a better time to sort of exit the asset. At the same time, we can continue to work with the sponsor, continue to maintain leasing at this asset, and like I said, look for a better capital markets exit.

**Rick Shane**
Got it. Patrick, so two follow-ups to that. One is that you guys have made the comment that it is covered on a cash flow basis, but that's on the senior side at the $120 million. Would it have been covered at the prior coupon at the prior note size or does shrinking the note and shrinking the spread put you in that situation?

And then the other side of this is, and this is what I was trying to look up, was the loan on non-accrual before, so you will actually see a pickup in reported interest income because this loan goes from non-accrual to accrual even if it's smaller at a tighter spread?

**Patrick Mattson**
I'll take the second part first, Rick. You're right and observant there. We will see some pickup on this asset as we move it off of nonaccrual and the senior now will be a performing loan and so you'll see that flow through our net interest.

The asset prior to the restructuring was very close to a 1.0x DSCR. Clearly, with the recut here and the senior loan being smaller and at a lower coupon, that allows for excess cash to be captured within this asset and that cash then can be utilized very proactively to continuing the leasing efforts here.

**Rick Shane**
Got it. And I apologize to my peers. I'm going to ask one last question. Will there be a catch-up in the third quarter related to the reversal of non-accrued principal that was captured running through the interest line or anything like that? I just want to make sure there's no noise that we need to be thinking about.

**Patrick Mattson**
No, there's no recapture.

**Rick Shane**
Okay, thank you.

**Operator**
The next question comes from Sarah Barcomb with BTIG. Please go ahead.

**Sarah Barcomb**
Hi, everyone. Thank you for taking the question. So, we saw both the Boston office added to the watch list and the Mountain View office see that downgrade there. Both of those were originated post-COVID. And I'm hoping you can speak to the issues cropping up in that post-COVID office bucket, just given we've seen more issues, of course, in the pre-COVID bucket but starting to see some of those issues crop up. Can you talk about how expectations have changed for that group since, call it, early 2021 to now?

**Matt Salem**
Sarah, it's Matt. Thank you for the question and for joining us this morning. I can try to take that.

I don't think that, whether it's pre-COVID or post-COVID, the properties or the loans are experiencing anything particularly different. I think it's just an overall market illiquidity and fundamental softness as well as we just adjust to work from home and what the real demand is on office space. So, it's the same underlying theme that's impacting either when a loan was made pre- or post-COVID.

I would say our bar for lending on office certainly was raised materially when we think about the world post-COVID, and maybe that's what you're highlighting here a little bit. The Boston asset wasn't really a transitional asset. It was a fully leased asset. It's 90% leased today, so it was almost a stabilized office building and still is. It's just a question of value now with the market illiquidity and the cap rates have moved out.

The Mountain View one is a little bit different. That's clearly a lease-up strategy from origination. But just given the overall quality of that particular asset, this is not going to be subject to some of the same concerns around occupancy. And as we may have on some of the more generic office space in the market, this asset will 100% get leased someday. It's a very high-quality asset. It's just going to come down to how long that takes and what's the lease rate at that point in time. So hopefully, that gives you just a little bit more context to that question.

**Sarah Barcomb**
Okay, yes. Thank you for that. And then maybe just to move over to the other side of the balance sheet for a moment here, I was hoping you could speak more to how you're thinking about liquidity and capital raising in the current environment, depending on the messaging that we hear at the Fed meeting on Wednesday, just given the amount of office exposure that's still on repo, combined with the growing watch list especially for assets where we've seen more of a valuation reset and where KREF has lower net equity. And you also mentioned in the prepared remarks that the money center banks are pretty cautious. So, I'm just trying to gauge how you're thinking about your liquidity needs going forward. At what point would you tap the corporate debt markets, the Term Loan B markets? How are you thinking about that?

**Matt Salem**
Yes, I can take that. It's Matt again. I'd say first of all, we have ample liquidity, so anything we would do would be more opportunistic in nature. We're not looking at the market saying we absolutely need to do something. There's really no immediate need for liquidity right now. You can see we have $800 million of liquidity, so there's ample liquidity there.

I'd say number two, we're going to continue to monitor all these markets. They've recovered along with the broader markets. So, to the extent we find something attractive, we could certainly look at that. The one thing that's in the back of our mind is we did pay off our convert this past quarter. It was small but we paid it off. So, if there was an opportunity to term that out at some point in time down the road, we may look at a potential opportunity to do that. But overall, I'd say we're just kind of watching the market and waiting for a moment where it could be attractive, but really no immediate need.

**Sarah Barcomb**
Thank you.

**Operator**
The next question comes from Jade Rahmani with KBW. Please go ahead.

**Jade Rahmani**
Thank you very much. And good to see some positive updates on the office side. So, the first question would be how far along through the scoping of credit risks do you feel we are? Would you say halfway

is a fair assessment or much more long than that? I think you did take pains to mention that on the risk 3-rated office loans, you don't expect any negative surprises and that portfolio is well leased with long duration. However, we haven't touched on multifamily, hotels, industrial and even life sciences, where we've seen a few hiccups. So, can you just comment on that broad question?

**Matt Salem**
Sure, Jade. It's Matt, I'll take that. Thank you for joining.

Well, let's start with the office, because obviously that's much further along. I think with the office side of it, we feel like we are towards the end of certainly identifying where there could be potential issues. I don't think all the 4-rated loans end up migrating to 5 and this is a question of what happens with some of those as we continue to kind of walk down the path there.

As it relates to the 5-rated loans, that feels like we've got pretty sizable reserves against those and appropriate reserves.

The office, I think we've been pretty transparent. I think we've been a little bit more front-footed than some of our peers in identifying issues reserving loans. So, I think for us, we feel pretty far down the road, not finished but pretty far down the road on the office side.

As it relates to the other property types, I mean, it's hard to say. It obviously could be early because we haven't seen any issues there. And clearly, real estate values have changed across the board with the increased cost of capital. But the valuation changes have not been anywhere near as severe as what we see on the office side, which obviously is getting hit from fundamentals as well as higher cost of capital as well as capital markets and liquidity, so it's a little bit of a perfect storm there.

So, we're watching the portfolio very closely. But even if you look beyond our broader portfolio outside of KREF, we've got almost a $30 billion mortgage portfolio across all the different accounts that we service or manage. Really we haven't seen any issues outside of office. So, I think a lot of those property types are well positioned, and that's not to say that there won't be issues down the road because the debt burden is quite high today and so that will impact certain sponsors. But I don't think even if you have issues, I would doubt you'll see a level of severity that we're seeing on the office side, which again are kind of caught in that perfect storm.

So, it's a hard question to answer but we're certainly monitoring it. We just haven't seen anything in our broader portfolio or KREF's portfolio yet outside of office.

**Jade Rahmani**
And on the multifamily side, you mentioned the rent growth, 7.5%. I mean we have seen multifamily performance being pretty resilient so far. Nevertheless, for those loans to be able to successfully refinance, we're seeing some interesting dynamics where lenders are providing preferreds in order to have the LTV meet other senior lender requirements because the preferred gets counted as equity. Do you think that the multifamily deals can stomach a 6.5% or 6% type interest rate?

**Matt Salem**
I think there's a timing issue there and the question is: what's the long-term tenured rate? I think there's a lot of sponsors today that are looking at their multifamily assets and trying to basically bridge the period of time from now to when you get into a little bit lower interest rate environment, at which point, they're going to feel pretty good about the value of their asset. And the question is, does your sponsor have the liquidity to bridge that gap?

And there's going to certainly be business plans that are in the middle and they're in the middle of renovating and upgrading units that people will get caught in this a little bit is my view. But I'd say, at least our portfolio within KREF, we feel pretty good about it. It's mostly Class A real estate. It's in liquid markets.

And the one thing that always surprises me about the multi sector is the amount of liquidity there. There is a tremendous amount of liquidity on both the debt and the equity side. And I think that’s propped up values a little bit and muted some of the issues that may be under the surface on the multi side. So, I think to answer your question directly, I think that cost of capital is more temporary, and so people are thinking about it on a more intermediate basis.

**Jade Rahmani**
Thank you very much.

**Operator**
The next question comes from Don Fandetti with Wells Fargo. Please go ahead.

**Don Fandetti**
I was wondering if you're seeing any opportunistic capital forming in the industry for office, whether it's on the equity or debt side? Obviously, sentiment has been extremely negative. Is that still the case or are you sort of seeing some green shoots?

**Matt Salem**
Don, it's Matt. I can answer that. I would say it's limited. I think part of the challenge with office is it's a large property type and most investors, whether you're a debt investor or an equity investor, you have significant exposure to it. And everyone is kind of dealing with their existing assets and reserving whatever capital they have with those. And it should be a pretty extraordinary investing opportunity, certainly given the illiquidity that we're seeing in the market today, but I don't think we're seeing really large institutional capital being raised around office.

**Don Fandetti**
Ok. Thank you.

**Operator**
The next question comes from Stephen Laws with Raymond James. Please go ahead.

**Stephen Laws**
Good morning. Patrick would love to follow up. I think you made a comment on the short sale in the Philly office. Can you maybe help us get a gauge of how much the specific reserve, of the reserve, it's roughly two-thirds on the 5-rated loans kind of applies to that? And is that a 3Q event or sometime over the second half as far as timing goes?

**Patrick Mattson**
Good morning, Stephen. We didn't give a specific number there, but if you look at what's implied by the numbers, you're talking about loss expectations that are potentially north of 25% on that asset and the other [5]-rated assets (corrected). We're obviously still working through that sales process and so I want to be mindful of that.

I think in terms of the timing, it's difficult to predict right now. On one hand, it feels like things are progressing well. And as Matt said, we're in the later stages here so there certainly could be a 3Q

event. But in this kind of market for these types of transactions to slip a couple of weeks or a month is certainly not impossible. And so, that's why we're seeing could be a 3Q event, but we would certainly expect it to happen by 4Q.

**Stephen Laws**
Great. Thanks for the color there, Patrick. And repayments came in a little higher than I was looking for, a good bit higher than I was looking for actually, but can you talk to that a little bit? It seems like you reiterated today kind of expect modest repayments over the year, which is consistent with last quarter. But it looks like maybe a multifamily asset in Florida, a small resi condo loan I think in Manhattan, but can you talk about what repaid during the quarter and any trends we can read into that?

**Patrick Mattson**
Sure, Stephen. You're right, we did have our condo asset, which is near Hudson Yards, had its last units sell and that asset paid off. There were three other multis that actually paid off. They were paid off through a fixed-rate refinancing. And so, we're continuing to see as some of these assets, in particular on the multifamily side, reach on their business plans a real opportunity to take coupons that are in the 8% to 9% when you look at the margin plus the SOFR index and refinance at a rate that's closer to 6%. So, we saw some of that activity.

And then we had a smaller number of partial repayments on some of our industrial loans, where there were asset sales.

And I guess one thing I would just highlight, Stephen, as we think about those repayments, those multifamily loans that paid off were certainly risk-rated 3. But if you recall, at one point, the condo asset was a risk-rated 4 asset and obviously, clearly was paid out at par here. So, a pretty good quarter in terms of repayments.

I think as we look forward, we still expect the back half of the year to be muted in terms of repayment expectations. And if we see those, I would think that they're more toward the fourth quarter as opposed to third quarter.

**Stephen Laws**
Great. Lastly, Matt, what are you guys looking forward to think about new originations here? I mean, it seems like you feel pretty good about having identified problems in your office and feel good about what's currently remaining 3-rated. Are you looking for rates to top out? Is it more macro? Or what are the deals look like that you're looking at the past couple of months you've decided not to do? And kind of what do you need to see improve to start doing those?

**Matt Salem**
Sure. It's a very interesting lending environment today, so I'd say we're very much looking forward to being able to get back into the market and create some new opportunities in the portfolio. I would say, really, it comes down to just working through some of these watch list items and just making sure that we get through them, we find a home, we get that equity returning to working. And then, it will come down to that.

And outside of that, I think once we're through that moment, then as we get repayments, we can go out and reinvest it. So that's really part of the reason why we have been more aggressive with dealing with some of these issues, identifying them, trying to get through them is because we very much want to make sure that we have the opportunity to take advantage of the current market environment. But it's going to come down really to the existing portfolio because I think what we're seeing in the market today is very attractive.

**Stephen Laws**
Great Matt – thanks for the comments this morning.

**Operator**
The next question comes from Arren Cyganovich with Citi. Please go ahead.

**Arren Cyganovich**
I was wondering if you could talk a little bit about the West Hollywood loan that you modified in June. What was the reasoning behind that and the outcome there?

**Patrick Mattson**
Sure. Arren, it's Patrick. I'll take that one.

The real starting point here was just the interest rate movement and the cap renewal that had to be executed. When we did the modification, as part of the modification, the sponsor agreed to put additional capital into the asset. So, in addition to buying a cap, added additional capital to help cover debt service, we agreed as part of the loan structure to add some additional capital as well that will help carry this asset through its initial maturity date, and as part of that modification, entered into some profit participation above our basis.

So, net/net, it puts the asset on sort of better footing for this current rate environment. The asset from an occupancy standpoint continues to operate in the sort of mid-80s here and that's something, obviously, we're watching closely. But at the end of the day, this is a really high-quality asset in a great location, and we feel really good about our basis here.

**Operator**
The next question comes from Steve Delaney with JMP Securities. Please go ahead.

**Steven Delaney**
Good morning, everyone. Thanks for taking the question. I was prepared when we started the Q&A or actually starting the call to ask you about the three 5-rated loans and if you saw any potential solution short of an actual foreclosure, and lo and behold, you've showed us two of the three you've worked something out, so congrats on that progress.

Just curious, if we were to look at this, I know these are moving pieces, right, both on the sale of Philly and the restructuring of Minneapolis, but maybe from a general perspective, as you look at those two transactions and the accounting as you move forward, you have specific reserves, I assume, on all these 5-rated loans. Do you think that your resolutions, as you model them out, your specific reserve will be sufficient to kind of net you out flat once those two transactions are recorded?

**Matt Salem**
Steven, it's Matt. Thank you for joining us.

Yes, I think that when we look at the sale and the modification, we think these reserves kind of match the current value expectations. I think that's a question you're trying to get through is I think we're appropriately reserved on those two assets.

**Steven Delaney**
Exactly. Will there be any kind of accounting issue, we all struggle with this, the gap and then the distributable, do you think these transactions will there be a distributable impact that the analysts that

we should be thinking about with respect to modeling? Jack, we can follow up off-line. I'm just trying to understand and get it out there, is this going to be an issue with respect to distributable beyond the fact that you're well reserved on CECL?

**Matt Salem**
Yes. I mean, if we have a loss, the CECL is going to translate through to DE. I think we mentioned that on the prepared remarks as well. So the most obvious one is if we get to a sale on Philly, our CECL reserve, where we think we're appropriately reserved, will flush through, if you will, DE at sale and we'll see what we get to. But yes, at some point in time, you'd expect some of these CECL reserves to be realized.

**Steven Delaney**
Great. Now in the case like that you actually take a property back, let's say you foreclose on Mountain View, at that point, I assume you're going to hold it and you're going to operate it, optimize it for a year to a couple of years, that REO would come on at fair value. So, if you actually do foreclose, convert it from a loan to REO, is that also a situation where the REO would be booked at current fair value that could trigger a realized loss?

**Matt Salem**
Yes. If we went to title, like you said, we would value the asset and we would take a realized loss on the difference between our basis and that value.

**Steven Delaney**
Okay, great. That's helpful. And I guess this is not a question but maybe a request. So as these situations play out with respect to actual closings of these anticipated, it'd be great if you guys could consider an 8-K or maybe a press release just alerting the analysts and the investment community that that transaction is now closed. And therefore, like in 3Q, Matt mentioned, could it happen in 3Q or is it going to slide to 4Q, we'd love to have the opportunity to tweak so that we're not out of line, if you will, with respect to where you see your distributable coming, your DE. So, I'll just leave it there, and thank you very much for your comments.

**Operator**
As a reminder, if you have a question, please press star then one to enter the question queue. The next question comes from Jade Rahmani with KBW. Please go ahead.

**Jade Rahmani**
Thank you very much. Just curious, if you have a borrower where you have multiple deals and one of the deals you're in discussions on, because it's having issues, do you make relationship-based decisions, or everything is case by case with respect to an individual deal?

**Matt Salem**
I mean, it's really a case-by-case basis, Jade. I mean, if we've got an issue and we're dealing with a sponsor, we very much are trying to optimize the outcome on the issue loan. So, I think we're taking those individually and seeing what kind of outcome we can get to.

**Jade Rahmani**
So, on Minneapolis, let's say the sponsor there has several other deals that they're not in the same position, but they could have some issues down the road that you're aware of and anticipating, it's just not at the same risk level, you're not going to talk holistically?

**Matt Salem**
It really depends. I mean, although you say same sponsor, in many cases it may be the same sponsor, but you have different funds or different equity capital involved, we may have it in different portfolios as well. So, to the extent it's just KREF on a bilateral negotiation with a sponsor that has the same equity base, and they want us to talk about a holistic solution, of course we could have that conversation. That's not typically how it goes. You're usually just in front of them on one deal and negotiating then.

**Jade Rahmani**
Okay. The second question, just to really put a fine point on what Steve Delaney was asking and also what Steve was asking earlier, the Philadelphia sale, the short sale, is that going to hit book value further than what's already reserved?

**Matt Salem**
It's not our anticipation. Nothing's done in this market until it's done, but we think we're appropriately reserved at the kind of current expectation of sale price.

**Jade Rahmani**
Okay. Thanks so much for taking the follow ups.

**CONCLUSION**

**Operator**
This concludes our question-and-answer session. I would like to turn the conference back over to Jack Switala for any closing remarks.

**Jack Switala**
Great. Thanks, operator, and thanks, everyone, for joining today. You can reach out to me or the team here with any questions. Take care.

**Operator**
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

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