Starwood Property Trust

Second Quarter 2026 Earnings Call Transcript
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Call Participants

EXECUTIVES

Barry Stuart Sternlicht
Chairman & CEO

Jeffrey F. DiModica
President & Director

Rina Paniry
CFO, Treasurer, Principal Financial Officer & Chief Accounting Officer

Zachary H. Tanenbaum
Managing Director & Head of Investor Strategy

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Presentation

Operator

Ladies and gentlemen, we apologize for the technical difficulties. Welcome to the Starwood Property Trust Second Quarter 2026 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded. I would now like to turn the floor over to Starwood Property Trust to begin the event.

Zachary H. Tanenbaum
Managing Director & Head of Investor Strategy

Thank you, operator. Good morning, and welcome to Starwood Property Trust Earnings Call. This morning, we filed our 10-Q and issued a press release with a presentation of our results, which are both available on our website and have been filed with the SEC. Before the call begins, I would like to remind everyone that certain statements made in the course of this call are forward-looking statements which do not guarantee future events or performance. Please refer to our 10-Q and press release for cautionary factors related to these statements.

Additionally, certain non-GAAP financial measures will be discussed on this call. For a reconciliation of these non-GAAP financial measures to the most comparable measures prepared in accordance with GAAP, please refer to our press release filed this morning.

Joining me on the call today are Barry Sternlicht, the company's Chairman and Chief Executive Officer; Jeff DiModica, the company's President; and Rina Paniry, the company's Chief Financial Officer. With that, I'm now going to turn the call over to Rina.

Rina Paniry
CFO, Treasurer, Principal Financial Officer & Chief Accounting Officer

Thank you, Zach, and good morning, everyone. Our distributable earnings were $152 million or $0.40 per share in the second quarter. Our results continue to reflect the carry on our nonaccrual and REO assets and elevated cash balances, the two items which are creating the gap between our reported earnings and the true underlying earnings power of this company. I will start my remarks by addressing both.

Regarding our nonaccrual and REO, we had no new nonaccrual or new 5-rated loans in the quarter or the year. We also had no new REO in the quarter. As our new nonaccrual and REO loans have slowed, we have gained momentum in resolutions. To clarify, our definition of “resolution” means disposition of the asset in the case of an REO or returning to accrual in the case of a nonaccrual loan. It is not the transfer of a loan to REO.

We have a total of $706 million of reserves against our nonaccrual and REO assets, after recording an increase of $30 million in the quarter due to third-party model macroeconomic conditions, which worsened as a result of the rise in interest rates. This consists of $485 million of CECL and $221 million of REO reserves, which translates to $1.97 per share that is already reflected in today's undepreciated book value of $18.62.

As we continue our efforts to resolve these underperforming assets, we are currently under contract or in discussions to sell three REO assets and multiple units in our New York City residential project. In aggregate, these sales are expected to generate cash proceeds of $148 million and resolve $195 million of assets on a DE basis and $160 million on a GAAP basis in the third quarter, comprising 10% of our current nonaccrual and REO balance. One of the three assets was re-traded recently due to rate increases, resulting in a $12 million divergence from our GAAP marks. Absent that, our GAAP reserves were in line with the anticipated sales price, demonstrating our ability to fully resolve these assets consistent with our estimates. The realized loss will flow through DE upon sale in Q3 and totals approximately $47 million for these assets. As a reminder, when assets are resolved at our carrying value, their reserves naturally progress to DE, but the reserve is already accounted for in our book value. Reinvesting these proceeds would add approximately $0.03 to annual DE as we continue on our path to earning our dividend in our core businesses.

Our total nonaccrual and REO portfolio stands at approximately $1.9 billion on a DE basis at quarter end, not including the $706 million of reserves that are already reflected in book value. Subject to market conditions, we are on track to resolve approximately $800 million, or 40%, of our current nonaccrual and REO by year-end.

Regarding elevated cash balances. We were especially active in the capital markets this quarter, issuing $1.1 billion of unsecured senior notes and upsizing our term loan B by $275 million. Offsetting this elevated cash was our accelerated investing pace as we deploy capital of $2.5 billion across our businesses and another $1.7 billion in July, bringing year-to-date investments to $6.7 billion.

I will now take you through our individual segment results, beginning with Commercial and Residential Lending, which contributed DE of $186 million for the quarter or $0.49 per share.

In Commercial Lending, we originated $1.4 billion, of which we funded $754 million and another $250 million of pre-existing loan commitments for a total of over $1 billion funded in the quarter. After factoring in repayments of $447 million, our funded loan portfolio grew to a record $17.3 billion. We received another $554 million of repayments in July, approximately $170 million of which were office.

I previously mentioned the absence of any new REO, nonaccrual or 5-rated loans this quarter. Our 4-rated loans increased $212 million to $2 billion, reflecting the downgrade of three multifamily loans that Jeff will speak to.

Turning to Residential Lending. Our on-balance sheet loan portfolio ended the quarter at $2.4 billion, up $164 million, driven primarily by our decision to exercise the call option on one of our securitizations, moving the majority of the financing to more attractively priced repo at SOFR plus 150. As a result, our retained RMBS portfolio declined to $313 million at quarter end.

Turning to our Property Segment. We recognize $34 million of DE, or $0.09 per share across our legacy and net lease portfolios.

I will start with Woodstar, our Florida affordable multifamily portfolio. On July 1, we began rolling out the new authorized HUD rent increases of 8.4% that we mentioned to you on our last call. The related earnings impact will appear in our results starting next quarter. The discount to market rate rents across the portfolio is 38% on average, which should ensure continued high occupancy and allow us to push through most of these rent increases.

Also in Woodstar, we have $416 million of Woodstar debt maturing over the next 6 months that we are currently working to refinance. Given the appreciation and NOI growth in this portfolio, we are anticipating an upside of approximately $140 million at attractive spreads, our $110 million share of which can be reinvested to increase future earnings.

In net lease, where DE increased to $0.05 from $0.03 last quarter, we closed $179 million of purchases in the quarter at a blended cap rate of 7.39%, bringing our total post-acquisition purchases to $532 million at a blended 7.45% cap rate. The portfolio now stands at $2.7 billion, comprising 527 properties across 44 states, a weighted average lease term of 16.8 years, average annual rent escalations of 2.3% and 100% occupancy with zero defaults.

Included in our balance at June 30 are $91 million of build-to-suit projects still under construction, with $65 million of incremental costs to complete. All of these projects are subject to executed leases. Upon completion of construction, these leases will add $9.9 million of annual base rent to revenue.

We continue to optimize this platform's capital structure, completing another ABS transaction after quarter end, our third securitization since acquiring the platform a year ago. The ABS financing totaled $321 million at a weighted average fixed rate of 5.47%. With our continued optimization of the capital structure, our first year of rent escalations in place and our investing pace, we continue to build toward the earnings power embedded in this platform.

Concluding my business segment discussion is our Investing and Servicing segment, which contributed DE of $42 million, or $0.11 per share, to the quarter.

Special Servicing fees were $20 million this quarter with the decline from last quarter due to timing of resolutions.

Our conduit, Starwood Mortgage Capital, securitized $320 million of loans, more than double last quarter's volume, at profit margins that were in line with historic levels. I will conclude with a comment on this segment's REO equity portfolio, which now has just 5 assets remaining. We sold one asset during the quarter for a DE gain of $2 million.

Turning to liquidity and capitalization. Our current liquidity stands at $1.2 billion. This does not include liquidity that could be generated from cash out refinancing, sales of assets in our Property Segment, direct leveraging or expected proceeds from REO sales, which as I've mentioned, could be relatively material.

Jeff will discuss the capital markets transactions we completed in the quarter. There is one item I would like to highlight regarding the early redemption of our $500 million January 2027 unsecured debt, which was subject to an interest rate hedge. In order to minimize interest rate risk, our policy is to hedge floating rate assets with floating rate liabilities and fixed rate assets with fixed rate liabilities. When we issued these notes in 2022 to a fixed coupon, we entered into a received fix/pay floating interest rate hedge to lock in SOFR plus 295 as the financing cost. In connection with the early redemption, we unwound the hedge. Due to higher interest rates today, this resulted in a loss on early extinguishment of debt of $6.3 million, which will be reflected in both GAAP and DE in the third quarter. The amount represents the present value of receiving the below market fixed rate through maturity. It is the onetime cost of retiring and above current market SOFR plus 295 obligation and replacing it with 5 7/8% paper, which if issued today would be 6.5% to 6.75%, saving us over $15 million over the next 5 years.

We continue to operate at conservative leverage levels, ending the quarter at a debt to undepreciated equity ratio of 2.74x. Our unencumbered asset pool stands at $6.9 billion against $4.5 billion of unsecured debt, a coverage ratio of 1.5x.

And finally, this morning, I wanted to conclude with a few remarks on the recognition we received this quarter by the rating agencies and Nareit.

During the quarter, both Fitch and Moody's affirmed our ratings, at BB+ and Ba2, respectively, collectively recognizing our diversity, leverage profile, liquidity position stable earnings and credit track record as key elements supporting our rating.

We were also once again awarded the Nareit Gold Investor CARE Award, an award given to one company in each industry, which recognizes as communications and reporting excellence. This is our tenth time receiving the award in the mortgage REIT category in the last 12 years, exemplifying our long-term commitment to both our stakeholders and transparent financial reporting. We are honored to once again be recognized by Nareit for this award. With that, I will now turn the call over to Jeff.

Jeffrey F. DiModica
President & Director

Thanks, Rina, and good morning, everyone. Despite a volatile macro backdrop, we've accretively deployed a near record $6.7 billion year-to-date. The breadth of opportunity across our global platform continues to grow. Higher rates have been partially offset by tighter credit spreads and activity has remained robust. CMBS issuance is tracking near multiyear highs, and CRE transaction volumes continue to recover gradually but steadily. The breadth of opportunity across our global investment platform remains as active as it has been since 2021. We have strong pipelines across our businesses and across continents, and we are on pace for a record year of investment activity across our cylinders, supporting the continued growth of our portfolio.

In volatile markets, investors have the opportunity to step back and examine the effectiveness of different business models. Our company has consistently outperformed in times of stress over our 17 years. We have said repeatedly that we built and diversified this company to operate through cycles and across macro environments, and the last 5 months have tested that thesis. Our unique diversified business model with only half our revenue coming from CRE lending has again absorbed this volatility. We see improving conditions in commercial real estate with higher absorption, less supply and more transaction activity. Our lack of credit migration and outlook again showcase the durability of the platform we have constructed.

In our Commercial Lending segment, our best-in-class financing and access to liquidity, which I will discuss more later, have allowed us to deploy near record amounts of capital this year. The third quarter looks to be our strongest origination quarter, reflecting the strength of our global origination platform and further diversifying our business.

Despite the leveling off of credit deteriorated loans, as Rina mentioned, we did have three multifamily loans moved to a 4 risk rating during the quarter, a $73 million multifamily asset in Phoenix, Arizona, a $63 million multifamily asset in Clearwater, Florida, and a $74 million multifamily asset in Mesa, Arizona.

These downgrades reflect the effect of higher forward rates I mentioned, and broader softness in certain Sunbelt multifamily markets where elevated supply that is mostly behind us has put pressure on near-term cash flow. We have over $6 billion in multifamily loans, representing 20% of our balance sheet, and more than twice as large as any other exposure. Despite this being our largest asset class, it is a relatively low percentage of our reserves.

We have increased occupancy and improved performance on assets we have taken back, in some cases, materially, positioning us to begin exiting them as we have before in a more thoughtful way that returns the highest return to shareholders. As Rina said, we expect over $800 million of resolutions in the second half of 2026, with the majority coming from REO sales on multifamily assets under PSA or actively being marketed, the redeployment of which will generate DE for shareholders.

In addition to the REO sales Rina mentioned, I want to point out a few additional positive credit outcomes in the quarter. We had previously told you about a $300 million office building in Brooklyn. During the quarter, the borrower signed the third and final lease for 32 years to a credit tenant, bringing the building to 100% occupancy with 30 years of WALT, allowing the remaining portion of the loan to return to accrual status and putting the borrower in a position to refinance or sell the property.

Subsequent to quarter end, two office loans repaid at par for $171 million in total, reducing our office exposure in the U.S. to just 7.6% of our assets, and globally to 8.9% of our assets, both the lowest in our company's history and an important indicator of lower potential losses.

Turning to our Infrastructure Lending segment. In the quarter, we committed $441 million of returns consistent with historic levels. After similar size repayments, the portfolio ended the quarter at $3.1 billion.

With the pricing of our seventh SIF CLO this year, our infrastructure loans benefit from term, non-mark-to-market financing on 75% of our assets, reducing funding volatility and improving our overall cost of capital in this segment.

The SIF loan portfolio benefits from outstanding credit quality. 92% of the portfolio was rated 1 or 2 by our internal review process. It has been 10 quarters since we downgraded a credit to watch list status, and our portfolio today only has one watch list credit with a $16 million market value. 97% of our loans benefit from public or private Moody's credit ratings, and 2/3 of those loans are rated Ba3 or higher. The risk-adjusted returns on this portfolio add tremendous value to shareholders.

Additionally, we acquired an asset in our infrastructure lending business via a debt for equity swap on a defaulted loan in 2019. As part owner of the asset today, we are under contract to sell it in the second half, for a material gain to DE and book value. We will tell you more about it in the coming quarter or 2 once consummated.

In our Property segment, our 1200 K Street Office to multifamily conversion received residential conversion permits in June, and we have completed demolition and started construction in a market where we have seen Class-A rents rise significantly since beginning this conversion process, which we expect to complete in 2028.

In our Investing and Servicing segment, our active special servicing portfolio, a key indicator for us on the future segment profitability, increased by $1 billion in the quarter to $10.9 billion, with new SASB transfers totaling $1.3 billion coming in. Our named servicing portfolio stands at $93.6 billion, and is the pipeline that will increase our active special servicing portfolio over time. I also want to recognize Adam Behlman, the Head of REIS and our SMC conduit lending businesses. Adam was recognized by CREFC as the recipient of the prestigious Founders Award, and we want to congratulate him on this well-deserved recognition for his leadership of our REIS business. Congratulations, Adam.

I want to finish with our capital markets activity because I believe it's one of the most important stories of this quarter and the last 18 months, and one that I think is underappreciated by the market. In the second quarter alone, we executed $2.1 billion of corporate debt transactions, including $1.1 billion in senior unsecured notes that were the tightest priced financial sector unsecured notes of 2026 for a high-yield bond issuer, $600 million that was swapped to SOFR plus 222 and $500 million at 5 7/8% fixed. We also executed a $275 million Term Loan B upsize and a repricing of our $696 million existing term loan to SOFR plus 200, which was 25 basis points inside our prior pricing. Subsequent to quarter end, we repaid $400 million of maturing July 2026 high-yield notes and early prepaid $500 million of our January 2027 high-yield notes, as Rina mentioned.

We don't have any more corporate debt maturities until July 2027. Importantly, these transactions extended our weighted average corporate debt maturity significantly to 3.7 years, nearly double what it was before the $6 billion plus of capital markets transactions we've executed in the last 18 months, while we also reduced the weighted average spread of our debt.

Finally, as Rina mentioned, Fitch and Moody's both affirmed our credit ratings in the quarter, a signal of the institutional confidence in this platform that underpins our ability to access capital at the lowest financial services spreads in the high-yield market. We repurchased $30 million of our $400 million approved stock buyback year-to-date. Management and the Board own over $350 million of stock alongside our shareholders, more than all our peers combined. Our investing pipeline is robust, and we believe in the long-term value of this platform and are confident in our earnings trajectory over time.

We've been telling you for years that access to capital at scale is one of our defining competitive advantages, and this quarter is a concrete demonstration of that. We are not a pure-play mortgage REIT and are, in fact, only half a mortgage REIT. This is why our results and trajectory are different. We are a diversified finance company with over $32 billion of assets, eight distinct business lines and the broadest access to capital markets of anyone in our peer group. The ability to invest accretively and in scale every quarter, and to issue high-yield notes, upsize and reprice term loans, execute CLOs, ABS, and CMBS conduit securitizations across multiple asset classes.

Our signaling is also unique and differentiated at a time when the traditional mortgage REIT model has come under pressure due to continued credit deterioration and lack of investor confidence, and it is a competitive moat that compounds to our company and shareholders over time.

With that, I'll turn the call to Barry.

Barry Stuart Sternlicht
Chairman & CEO

Good morning, everyone. Thanks for joining us. The first item of my day is to wish Rina Paniry a happy birthday. Happy birthday to you. The first management team to sing to their CFO. Maybe that's a violation of SEC decorum. I don't know. We'll find out. A little surprised by the stock's reaction this morning. I think we actually had a pretty good quarter and not deviant from anything we've talked about.

I think we're kind of throwing the baby out with the bathwater. Remember, half our company is not large loan lending anymore. And I'm sure there's worries in the world about the stability of these mortgage folks given our competitors' reports heretofore. So, I think we look at it differently, and it goes to, of course, our dividend, which we're very public about and you could see we're not covering. We're pretty confident in our ability to get back to the earnings power that we'll need to drive the dividend and restore our coverage of dividend.

And why are we confident? So let's start with what's actually happening at the property level in the United States today. Almost all the real estate asset classes here and in Europe are in repair. I mean everything is getting better. If you look at all the equity REITs in the multifamily sector and logistics sector, self-storage, senior housing, everything is getting better. That's basically driven by steady demand and rapidly deteriorating or nonexistent supply. I think retail construction is like less than 1%. Office is at historic lows. If you take out build-to-suits, there's almost nothing being built in this country, apartment starts dropped 70%. Logistics starts down 70%.

And you're beginning to see improvements in rent in the multi-sector, which we've been waiting for, God knows, how many quarters. But the markets are absorbing. There's still new supply completing and things are getting better market by market. Basically, the weakness is in the Sunbelt cities, and it's pretty strong on the two coasts, given nobody was building in California or New York City. And now it's even harder with the rent -- the prospects of rent control in those markets. So, the bad news is for the whole sector on the legacy books are the flattening of the yield curve, but interest rates have gone up.

So, we have a lot of multi's that borrowers are saying, I'll survive for '25, lower rates will allow me to refinance, and I can hold on for what we know will be pretty good years if you listen to Camden or UDR or AvalonBay, or Essex. I mean, they're all different geographies, but they're all talking about a pretty good year in the back half of '26, and really good in '27, and stupendous in '28 is the kind of comments from those management teams. A lot of borrowers were holding on for that. They're not making a lot of money. They didn't -- but they're paying their debt service. So now it's getting a little more challenging for these guys because they're not refinancing at a 3% SOFR. They're refinancing at a 4% SOFR, 4% and 1/8.

I actually fundamentally, can't really understand the Fed's position on raising rates to this economy. It's not going to open the Strait of Hormuz. It's not going to change the price of oil in the United States. It will only impact the interest rate sensitive portions of the economy. Looks like a broken record, almost 1/3 of the economy is really health care, education and government hires. Those sectors have added almost 6 million jobs since the Fed started raising rates 500 basis points in May of '22. It doesn't work on this economy. I listened to these bubble heads on TV in the morning talking about the manufacturing sector. It's 12 million jobs. It's irrelevant to the United States economy today. We need to bring back manufacturing and how are you going to do that with a 4% unemployment rate.

Most people like working with service economies. So it's really a funny concept, but it is a tax. The rise in oil price is a tax. The proper move might actually be to lower rates in order to induce the interest rate sensitive sectors like housing to be affordable and to recover and to take a burden off the consumer, that increased prices represent to the consumer.

So, I would say the backdrop is it's getting better at the property level, which fundamentally is important. And the other big news, obviously, for our shareholder base this morning is we are very busy investing capital. The opportunity sets are great. We're having record flows of investments. They're double-digit yields consistent with everything we've ever produced in the past. And this is all new stuff, and it's obviously becoming a bigger and bigger portion of our book going forward. So, what we have to do is nurse the older stuff. And we're pretty confident of our ability to turn what doesn't earn much or almost nothing, some of the assets we're getting back, into being able to sell them and return the capital to invest at these double-digit returns, which will ultimately support the dividend.

And I'll give you a few examples in our book and what you see -- probably don't appreciate and Jeff kind of mentioned it, but I'll double dip on the comment. When our borrowers get stressed, they stop investing in these assets, and they kind of -- in some cases, they can't even -- they don't put the money to turn the apartment units. They're actually trying to strip what they can before they give it back to us. They stop CapEx. Another property, they didn't do elevator repairs, so you couldn't get to the units on the top of the property. One property we did foreclose on, which is a mixed-use development in Texas. Our team, since we took it over like 3 months ago, has taken the NOI of the hotel from $1.2 million to $4.6 million. The apartments, which we had to fix the elevators in, have gone from 60% to 80%. We're

confident we'll get that into the 90s and the hotel will stabilize probably in the 7%, 8%. We'll get out of this hole in my opinion.

But at the moment, it's certainly not much for our shareholders. So we're an equity shop. These are equity assets. Our capital is an equity shop. I always joke to our team. It's really fun to get these multis back because you're getting them back at a really good price per key. And if I was an opportunity fund, I'd buy them. And we are selling them. We're getting them back and within a month or 2 or 3 months, they're gone. In fact, we fix it, we just sell it and we don't lose money. They could lose $5 million or $10 million, it's completely irrelevant to the company as a whole.

And in some cases, we might actually make a little bit of money. We're seeing cap rates – there's a portfolio of apartments that just sold in like a week. It will trade in the 5.2%. It's a very large deal, and you did it with almost no due diligence. So there's great appetite to buy apartments, which everyone knows what's coming down the road and you see this across the whole country. In fact, we've been bidding on apartments on the West Coast. Cap rates are dipping below 4.6% or 4.7%. We have a bid of 4.3% on an apartment deal in Florida. So the cap rates are there to support these loans, but we have to work through it. There's no fast answer here. And the resolutions of these deals is not always in our control.

So we have to take it back, we have to minimize transfer taxes, if it's in the states with transfer taxes. But we're confident in our ability to restore the earnings power of the company in the near term, although that could take a little longer than we would like. And so we think we're not considering our dividend -- changing our dividend policy at the moment.

If things go differently, if something interrupts that we don't know about and we see, we'll have to revisit that. But right now, we're confident in our dividend. And as a shareholder myself and the management team, we know exactly what we're doing. We're obviously overpaying our dividend. We're deteriorating our book value slightly. But we believe our shareholders have wanted to see consistency and transparency, and that's why I'm talking so much today to actually tell you what is actually going on.

And we look at our book, I can break it down between the really good stuff, the stuff that's eh, and then the stuff that's not doing much. And to us, it represents just tremendous earnings power. And we're going to look, if we have to take small losses to redeploy that capital now and get to the 12s and 13s and better that we can produce on the capital when we get it back, we're going to do it.

And we'll just do it measurably. And we have gains in our book. So we can offset some of the losses with gains and you know where they are. We've talked about them for the last 13 years. And that stuff is only getting better. So when you break down our businesses, look at our really good stuff. Obviously, our infrastructure business has been terrific. It continues to be great. Our special servicer, our conduit, our Resi book are all fine, Woodstar, our apartment portfolio, terrific. Our triple net lease business, not adding much to our earnings right now, but I look at it as an opportunity because we have a business that trades at a 6%, a triple net lease business, 17-year leases, 0 defaults. It trades at a 6% in the public market, and it trades at 11% or 12% dividend yield in us, and that's dumb, right? We're not that stupid. So we have to look at what we can do here. We love the earnings. I mean, the stability of the earnings. We love the depreciation shield it gives us, but we have a large business inside of us that would be worth materially more if we sold it.

And if we sold it or we somehow spun it off, we did something with it. We obviously think we could enhance our earnings profile. It's not something we really want to do, but it's something we know that we have in our pocket that we could do if we could figure out the right way to do it. So, I'll give you one other REO story because I actually just visited the asset in Washington, D.C. We took back an office building from one of the top three or four real estate sponsors in the United States, a company that most people -- actually, this particular company is, even though we've taken multiple buildings back from them, they've never reported the defaults and the losses they've incurred in all these assets, which is fascinating.

But leaving that to the side. This former office building we inherited, we've got approval and we've begun the process of turning it into an apartment complex. I looked at -- we already started. Rents have gone up in D.C. What we thought would just get us our capital back, now possibly we could make money on -- there's no way to accelerate this. Like, it's a

couple of hundred million dollar assets sitting on our books, you're giving it 0 value because it's not there to produce the dividend. It is a work in progress. It will be finished. It will lease, plus or minus something and it would be an additive asset, and we'll get our capital back.

So I don't know how to do that any differently as you take the long view, which we have, we're the longest surviving firm in our space and the largest in our space. So we're going to do that. Other cases, like, we've restructured a loan on a portfolio of apartments. We might look to just sell the loan. It's fine. The loan to assets are definitely worth the loan balance, but it's underperforming. We can't materially increase the ROE on that loan. It was restructured and we agreed to a fixed rate loan. So it's under -- it's earning, but it's not earning the levels of returns we want to earn on capital of that scale in our company. So, asset by asset, modified loans, and nonaccrual loans, we're going through them all, and we're going to figure out the right way to maximize shareholder value and build back our book value.

So, I think I'm actually feeling pretty good about things. I really -- I'm looking at the future and all the earnings power of all these underperforming assets as well as our ability to put out the capital across our very differentiated platform at very attractive returns, consistent or better than we've had in the past. And we are going into a new line of business, which we'll tell you about next quarter. At least we're highly confident we're going into it, which will add another cylinder to our company.

And again, nothing to do with commercial -- well, income-producing commercial loans. And we continue to look at acquisition opportunities and opportunities to consolidate our sector as some other people throw in the towel and where stocks are trading at material discounts to book value. We should be a sector consolidator and still keep our eye on the ball, which is to try to make investment grade down the road. So our -- what Jeff and Rina and the team have done to our balance sheet is heroic. We have, by far, the best balance sheet in the sector. I call it a fortress balance sheet in our sector, with very little near-term maturities, we've lowered our cost of capital.

And if I'm right, which is a counterview that rates won't go up as much as people say, I think things will get better, continue to get better. So, unhappy that I can't tell you it's perfect today. Very happy that I can tell you how we can grow and restore earnings power, it’s pretty obvious to everyone in the room. And we're doing about what we told you we were going to do. So there's not much of a surprise.

It is nice to see we had no deterioration in our credit book. The CECL reserve just went up because interest rates went up and that's an economic model that we can't control. We have $700 million of reserves against this book. I'll give you a little hint. We'll probably use a lot of that down the road. But that won't impact book value when that happens and -- when and if it happens. But again, things are picking up. I mean even the office markets are getting leases, which we've been consistent for now two years. The good buildings are leased and have tremendous rental power.

And even in our suburban book, in our equity book, not this company's book, but Starwood Capital's book, we're kind of surprised of the velocity of office leasing coming back to markets that we had considered to be weak. And the industrial markets. I can tell you, like, not getting away from this, we are quite busy in getting multiple bids again on industrial assets. All that bodes really well for the majority of our book and for the opportunities that we have in front of us.

So with that, I thank you for your time, and I hope you have a great rest of summer. And I know you joined me in wishing Rina happy birthday. Thank you.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Jade Rahmani with KBW.

Jade Joseph Rahmani
Keefe, Bruyette, & Woods, Inc., Research Division

From an equity perspective, when you're bidding on multifamily, you mentioned the 4.3% cap rate on the California portfolio. How are you thinking about that? Is there an opportunity to create rent growth and there's supply shortfalls down the road. So the fundamentals are really going to turn the corner. Is that the thesis there? Because I think multifamily has been challenged with taking a lot longer to turn the corner on rent growth. And now with the recent spike in interest rates that potentially weighing on valuations.

Barry Stuart Sternlicht
Chairman & CEO

So the 4.3% was actually in Florida. It wasn't in California, but we bid on some apartments in the Bay Area, and I think the cap rates were 4.5%. We lost, by the way. We're seeing 14% lease trade-outs in the Bay Area. So like this is in both renewals and new leases are positive. You see across the country, both in SFR and in apartments that renewals are positive and the propensity of people to stay is higher than it's been in the past because there's no work for them to go. They're not buying houses. So that's been good. They're positive, but the new leases have been challenged. And what we're seeing is concessions are burning off, and that's the first thing you see before market rates go up. So instead of 3 months or 2.5 months or 2 months or 1.5 months, that translates into rental growth actually, effective net rents are going up.

And I think it is market by market. I think the Northern Florida market seems to be turning a little faster than some other markets. And even in a city like Austin, which is probably the worst apartment market in the country, we have assets that are positive on both renewals and new leases and others that are down material. So I think it's totally -- right now, it's like the stock market picking. You pick your market, you pick your asset in the market, you pick your ZIP code in that submarket. You see a lot of the new construction of data centers and to some extent, manufacturing facilities, if you're so lucky to have an apartment building near one of these, you have a great pricing power.

You saw the hotel companies talk about the lower end of the market getting better. It's kind of consistent with that C-shaped economy. We're beginning to see this bottom turnaround, which we have not seen in our lower-end extended stay stuff, not stuff you own here. But Starwood controls 110,000 apartments, 60,000 affordable units and 50,000 market rate, and we get data trailing 30, 60 and 90 days in every market we're in from our portfolio. Obviously, with AI, now we're collecting data on everything else that comes in the shop. So for me, I'm an equity guy, we're sort of masquerading the debt world.

We wouldn't mind holding some of these assets if we thought they're going to take off. We've been trying to turn them quickly and get rid of the REO in the multi book. But at the time, I turned to our team and say, why are we selling at that price per unit? It's half of replacement cost. So I think -- I don't -- it's funny. My own team showed me a REIT the other day that they classified as an office REIT. This office REIT is really an apartment REIT so the market thinks they're an office REIT. It's still classified there; about 80%, 70% of their income from apartments. We're a mortgage REIT, you're treating us like we're just a mortgage REIT. Even if I took back all this equity book, you'll still treat me like a mortgage REIT.

So, I want to make money for the shareholders. I want to own these assets, but as a mortgage REIT, I should just get rid of them. So, we could convince people like half part of us is -- equity REITs and are trading probably at a 4.5% dividend yield, not a 12%. And our high ROE businesses, which is our servicer, the nation's largest, $100 billion of loans that in

services and almost $10 billion in a special right now, that is a great business. I mean it's a fantastic ROE business stuck inside of us. No one else has one, and we get no value for it in our current structure. We're treated just like everyone else. And no one else looks like our company, not even remotely close. A few have pivoted to try to build some of these verticals, but they're irrelevant given their scale. We're half other things, right?

So, we have -- and for that reason, you'll see us get more aggressive on our stock repurchase programs. And personally, we'll see what we do. But we don't get gifts like this every day. So I think we represent a pretty good value in a very volatile world where obviously, we're in the data center business ourselves. We probably have $20 billion, $30 billion deployed in that sector. So we're a lender to the sector in the business. But that is a crazy business right now, people. There's a moratorium going up for review, I guess, in Dulles County, which is the largest data center market in the world. It is so big, it is bigger than all of Europe and Asia combined. It's been the king of data centers. And all of a sudden, they seem to have caught the political headwinds of “not in my backyard”. So it is sort of pregnant on data centers, the 8.5 gigawatts on their way to, I think, 10 or 12. So it's like that business is getting airy.

And we have stocks that are trading at all-time highs, assuming all these data centers get built. They better hurry up and get space ready because in the United States, whether it's Chinese influence or not, is getting it really hard to get approvals for data centers. And I think the market has adjusted not a basis point for a slowdown in the ability of us to get all of us in the development world to get these data centers approved and up and ready in time.

And it makes those that are approved, even more valuable. But I think -- look, the volatility of the world has always been good for the real estate sector. Real assets are someplace everybody wants to come, and real estate loans are pretty attractive relative to tech credit where I laugh. I was talking to one of my children the other day. I said, at least you go to bed knowing a garage in Mongolia isn't coming up with a new LLM that's going to put us out of business. I mean the pressure of our business is different, right? Like we're not -- we don't really care about a building built in Tokyo, right? And if you're in a tech world, you can go out of business literally overnight. And this sector, we're resilient. We're the world's largest asset class, and there's always something to do. Our job is to go find out where the good risk returns are for the least risk, and we've built a company that has lots of ability to deploy capital into other things.

We've been looking at other things, too. We're very careful, and we have the SIF team brought us a very interesting transaction, which we may or may not go back and do, but that we're looking at doing what we're supposed to do, which is build a consistent earnings stream and be transparent. And I think the shareholders do appreciate that, and that's why we've got Nareit’s award for 8 years, 10 years in a row, so most -- best reporting, probably these earnings calls, too.

Jade Joseph Rahmani
Keefe, Bruyette, & Woods, Inc., Research Division

I mean, is there anything that you've experienced this cycle that changes your views on how Starwood Property Trust should invest? For example, the regional banks have pulled back materially, does that open up an opportunity in perhaps fixed rate lending, attacking the middle market and also liability management. I think the mortgage REITs you mentioned that are under so much pressure, it has to do with their liability structure, which makes them a forced seller in many cases. Starwood has been wise to diversify and continue to diversify the right side of the balance sheet.

Barry Stuart Sternlicht
Chairman & CEO

Yes. Like the new business we'll talk about next quarter is actually a business that the bank -- regional banks have left and or greatly reduce their capital allocation to and we think it could be a particularly good vertical for us going forward. We've been working on it, but we finally found a way to get in it. And I would say construction is interesting for us today. And I guess the other thing people need to be aware of, of course, is rising construction costs across the globe, in the United States are still in place. And one of our board members was -- we just recently had a Board meeting, I think it was last week.

And one of our board members is in the construction industry, and you've gotten reports from some of the housing companies that prices have come down. What's really happening is labor is becoming harder to get again because the electrician and the plumber are getting picked off to build the data center at 2x what they're getting paid to build a house.

So that applies to commercial real estate, too. All of the construction that's needed to build all this stuff, they're just stealing workers from other verticals in the economy and putting pressure on wages. Materials are okay.

We'll see where oil winds up because everything in a building is some derivative of oil, plastics and piping. Copper prices are pretty high. So I think you're not getting a big help there, but construction prices are -- it's not getting cheaper to build across the country and particularly in the union-dominated cities, it's brutally hard to make the economics work.

So I think -- I don't know. I mean we had three loans, I think we approved yesterday. We're still seeing lots of opportunity globally. Pretty constructive in Europe and continue to find good opportunities. And we've been through a lot of cycles in our 15 years, I guess. What I call credit cycles up and down our sector, and we continue to find opportunities to deploy capital. That's when you should be worried by the way. I mean you should be worried about us when we can't produce double-digit yields on the books we originate. We'll tell you when that happens. But right now, that's not the case.

Jeffrey F. DiModica
President & Director

And it's been fairly consistent, the yields that we're returning over the last 4, 5, 6 years, even on a levered basis. You said 2 things Jade, you talked about banks. And the banks coming back, it certainly helped our repo. We've talked about that ad nauseam, so I won't go there. But they are significantly better off lending to us from a regulatory capital perspective than making whole loans, and that's helped where we finance ourselves.

You also mentioned fixed rate lending. The insurance companies with a lower cost of capital and us, tend to lend fix. And when rates go up like this, they have a yield target and that tends to drive spreads lower because they're willing to lend at an all-in yield and that helps drive spread. Both of those things are helpful to us from a borrowing perspective, where we're borrowing at lower spreads. So we draft off that, but we're unlikely to compete in fixed rate lending away from the CMBS conduit world where we're doing a decent amount of 5- and 10-year fixed rate lending, and we're the #1 nonbank originator of CMBS for the last 2 or 3 years in a row. But most of these things create tailwinds to what Barry said, which is our pipeline that will continue to earn double-digit deal on. Operator, next question?

Operator

Our next question comes from Rick Shane with JPMorgan.

Richard Barry Shane
JPMorgan Chase & Co, Research Division

Barry, I have no idea what the SEC will say about you singing, but I believe that they put happy birthday in to the public domain. So at least Rina won't have to expense you singing to her this morning. One question for you. You alluded to -- not alluded to, but you started to talk about data centers. Starwood Digital Ventures has a partnership with MARA. I'm curious how we should think about how that partnership interfaces with Starwood Property Trust, how that partnership is going? And how you see allocation to data centers between equity and debt across the platform?

Barry Stuart Sternlicht
Chairman & CEO

For those shareholders, anyone listening doesn't know what we're speaking about, Starwood, on the private side, has a JV with MARA, a Bitcoin mining company where we are the -- we take their Bitcoin mine and we take over and turn it into a data center. They have a number of projects, and there's been tremendous tenant interest in their projects. There's no crossover between Starwood Property Trust and the activities of the Starwood Digital Ventures at the moment or the MARA partnerships. So they're totally separate.

But I think you saw the EPCOT moratorium in Texas. And that -- I think that's just a slowdown so they figure out what they're going to do. But getting approvals for deals has been harder since the public sentiments determined that data centers are evil. So even in Texas, it's put a kink in things. We do have unbelievable tenant interest in the properties. And I think for all of us in the data center world, we have to figure out what the credit profile is of some of the tenants.

There's obviously the -- we've only done deals with the hyperscalers, but even in the hyperscale world, you have a different credit of Oracle versus Meta or Amazon or Microsoft, and then we've not done any data center work with any of the neoscalers or CoreWeave or any of those guys.

And I think the whole data center world is being driven by the availability and proceeds levels and pricing of the debt because everybody is trying to do basically the same thing with the same half a dozen tenants. And some people are willing to build, it's funny. It's so new in the markets that -- I got a data center and you're like, “oh it's great”, but some of them are -- maybe they're building to 7, some may be building at 8, some people are building at 9, some people are building at 10. We built a data center to a 12. I mean it's -- you don't know. You don't know. You can't -- I was seeing one of you has written about another REIT, equity REIT, that's big in data center businesses, and they're making an assumption. Some of the analysts are on what the yields on costs are. There's no way you know that because nobody told you that, and a lease hasn't been signed, so how could you know. I think from our perspective is that our lending to that sector is very -- we're very comfortable where we are in the syndicates that we participated in, and we'll continue to look at the credits and make sure that we're comfortable with the credits.

And once these things are completed, they will be refinanced because, I guess, another view is whether you have a 15- or 20-year lease from a hyperscaler, and they're backed by their credit -- it depends what kind of data center is. But the real question is, why should their real estate credit be 500, 400, 300, 200 basis points wide of their corporate credit. And that's what the market sees. So there seems to be a tremendous appetite, at least in the public markets for data center debt, and you've seen some very large deals get done still in the market. And we're looking -- we look at everything. So what we want to participate in and not, typically today the spreads on a Microsoft deal won't work for us. We won't be able to make that.

Jeffrey F. DiModica
President & Director

But we were fairly early on, and we do have some much higher yielding data center exposure. Our largest one will pay off later this year. It's already out of construction. But the book that we put on, we're very comfortable with future funds to about $1.8 billion total of our $30 billion book, but it's a higher yield than you can get today.

Barry Stuart Sternlicht
Chairman & CEO

That's exactly the point is the finished data center gets refinanced and we get taken out.

Operator

Our next question comes from Chris Muller with Citizens [Capital Markets].

Christopher Muller
Citizens JMP Securities, LLC, Research Division

So I wanted to touch on the net lease business a little bit. The interest rate environment has shifted pretty dramatically since you guys first acquired that. We have 2 rate hikes priced in by midyear next year. So I guess, generally, how do you guys expect that business to perform in a rising rate environment? And maybe both on the demand side and the existing portfolio.

Barry Stuart Sternlicht
Chairman & CEO

We have -- we play in this space as a niche, which is sort of sale leaseback of core facilities usually associated with some transaction that's taking place. What we've actually seen is not what you would have expected with rising rates, and the cap rates are coming down. There's a lot of money chasing net lease. And we have a lot of peers that are raising money privately to compete. And we're scratching our heads on some of them because we can't understand the cap rates that they're buying at and the leverage they must be putting in place, how they could be producing the returns they're talking about. It's simply not possible, frankly.

I don't understand what they're reporting. This is other companies, not us. So our book steps up 2% or 2.25% rent bumps every year. We've got a great leverage structure in place with this ABS securitization trust, which we've done. And even in there, I think the spreads come down probably 50 bps from where we started and leverage levels have risen. So the ROE goes up because even though you're paying -- you're coming down in the cap rate, you're getting a little more leverage. It's match book.

Jeffrey F. DiModica
President & Director

And we end up 70 basis points or so off our warehouse facilities in the interim before they go to ABS.

Barry Stuart Sternlicht
Chairman & CEO

You're still super competitive, but we hear you. I mean, around the world, capital is looking for safe, high returns. And I think triple net lease is just a bond equivalent kind of thing.

You would think normally a long-dated bond would go down in value, but it's -- I think it's just still a quest for yield everywhere. And one of the enigma's of our businesses like Tokyo, cap rates are in the 3s, you all know what's happened to Tokyo interest rates, like cap rates are plummeting and they're plummeting because rents are going up. And I've always told our team, I mean, rents are more important than interest rates. If you think rents are going up, you're going to buy down the cap rate and you don't really give a hoot about a 0.25 point in interest rates.

So I think you'll see the same thing in properties. You won't be directly linked if there's significant growth. You see this today in the active senior housing, senior housing and you're buying down the cap rate because the growth is so strong. There's no construction. So the rise in interest rates, not -- believe me, we're in the market bidding on this stuff all the time and getting out bid all the time. It's really about rental growth. It's 3/4 of the underwriting.

And interesting, we lost these deals and probably regret doing it like for the apartments in the West Coast, some of these markets where they're going to -- when you see 10% rent increases, and of course, you deal with the prospects of rent regulation and everything else in the blue states. But you can buy down the cap rate pretty quickly because you're not worried about the cap rate or the yield being that same number 2, 3 years from now.

So you're right. I mean, I think our capital deployment, to be honest, has been slower than I hoped. It's been what they planned to be clear. But I kind of thought as we got more aggressive with our -- and our ability to finance the business, we could put out more money. And it's been steady, but not as high. And that's one of the reasons it's not as accretive as we had hoped earlier. We knew it would be dilutive when we bought it, but we thought we could get to materially accretive faster.

And that has not been the case because yields have come down. Cap rates have come down for the triple net lease and too fast for us, even though the financing has come down, it hasn't been enough to get to -- and actually, there's one thing you see, there's fewer buyouts, there's fewer deals because rates have gone up and people are scratching their heads on their terminal values and their multiples, are they right, are they wrong.

So it's solid, and it's a great business. It's just -- it's not been as accretive and obviously we issued stock to buy the company at a higher price. So, sort of unfortunate, but it's not a bad thing. It's just -- and again, it fits in our business, and you can look at the public comps and know what it would trade at. It wouldn't trade at a 12 today.

Operator

And our final question comes from Gabe Poggi with Raymond James.

Gabriel J. Poggi
Raymond James & Associates, Inc., Research Division

Happy birthday, Rina. Barry, Jeff, I want to go back to the comments thinking about look, Starwood Property Trust is a diversified commercial real estate business, period. You guys have been around for 15 years to the bellwether in the space. They got a lot of cylinders. How do you think about the world we live in now, right, still being bucketed as a mortgage REIT, having a net lease business, having Woodstar, taking on more REO. Barry, to your comments of “we'd like to own these assets for a long time”.

How do you think about that in the construct of right, cash flows, the dividend has been a constant since day 1, which you guys have talked about ad nauseam in a good way. But thinking about that? And then arguably, what's the best total return, right? If you had a book today, what's the best total return profile from an asset allocation perspective?

Is it making new loans, just cranking out 12s? Is it taken back keys on Sunbelt multi, waiting a few years, hoping -- not, hoping is wrong word. Fixing them. The market. The Iran conflict settles. Rates come down of skosh, et cetera, and there's a way to move those faster.

I want to get a dynamic of how kind of the big machine, Starwood Capital, thinks about what STWD can do while you play the long game.

Barry Stuart Sternlicht
Chairman & CEO

Yes, yes and yes. It's a really good question. I mean, we should -- maybe we can -- sorry, most of you follow the mortgage REITs, but maybe we could get some equity REITs analysts to follow us and move to our own little bucket. The bad news is we created a weird company in the capital markets. And you've seen other REITs diversify and sometimes they get -- it doesn't seem to pan out the way they hoped. I think if we were structurally going to change ourselves, that's something -- that's a very material strategic decision. And right now, we're supposed to be a mortgage REIT or I'd say, a commercial finance company or finance company. And I thought -- we're -- Jeff tells me, we're about 26% owned real estate today. I don't know if that's good or bad way to explain. In the Woodstar’s case, it's good news. When we bought those -- because we own the stock, I said these are things that I never want to sell.

They're -- how could affordable housing, again, rents do not go down. It's impossible. And they go up based on income growth. And over time, you're going to have income growth. And they have no real estate taxes. So we're not going to get pressured by municipalities. They're going to keep raising taxes to tax those wealthy people that own buildings. So they are just fundamentally a fantastic business. And look, it's not a 30% IRR business every day, but we made $2 billion in a trade for our shareholders, which Starwood Capital Group did. And it's given us appropriate opportunities to help ourselves with potential gains if we want to harvest them to help us offset some of the other challenges in the book.

But yes, it's a good question. We're going to have to think about this over time. And see how this all comes to fruition. We're not going to have the stock trade at 12 dividend yield. I mean that seems to be -- that's -- we can't -- that's sort of silly, why would we even do anything. That's why we'll go back in the markets and start buying stock again.

Jeffrey F. DiModica
President & Director

If you think it's 26% commercial real estate, owned commercial real estate, should trade at a lower dividend yield, which I think the world is telling you low income housing tax credit do, net lease does, the few multis we've taken back do, you're effectively implying 14% dividend yield on your lending businesses. Our lending businesses are performing in line with what we're telling you, and we have outsized return lending businesses like our infrastructure business, et cetera.

Barry Stuart Sternlicht
Chairman & CEO

Well, you know the markets, we're caught in ETFs. They're probably -- ETFs are getting redemptions. I'm sure that's part

of the issue with our sector. And we're big, so we get hit with redemptions as much as more than others. So we just have to distinguish ourselves over time. But Jeff makes a superb point, which I'll say again. So good. If 26% of your books should trade at 6, looks like, look at the cap rates of apartments are, which are 5's in the public market. Net lease dividend yields are 6. I think the underlying NOI's are 6 to 7 cap rates. To take that out, 6 or 7, there are mortgage books what, at 14% or 15%? That's ridiculous. So with this credit, what's our LTV exposure, 0 to what? 57. It's ridiculous. We have whole loans, and it's ridiculous, but that's okay. We have -- we're playing long ball. Sort of painful on the mark, and I fear for our shareholders, particularly the retail that doesn't probably understand what's going on as much and is nervous that we're going to go the way of some of the other mortgage REITs.

It's structurally not really possible right now the way we've built the company. So, we'll see how this plays out. But short term, I think some of our peers were a little more aggressive on the recovery of the straight line than they should have been and we too were surprised, by the way, by some of the reports of these other firms. But again, look at the amount of capital we're putting out and new stuff, 2.0 stuff, versus in the past record deployments. And then what did we put out already this quarter, you just said?

Jeffrey F. DiModica
President & Director

$6.7 billion for the year, $1.7 billion already closed in July. We should have the biggest origination quarter in a couple of years, this quarter.

Barry Stuart Sternlicht
Chairman & CEO

So I mean, feel really good about that. Again, when we can't tell you that, then you should worry. Right now, is not the time. You should look at it as a hidden earnings machine as we get this stuff back online. But gosh, it does just -- I can't get our team to build out those stuff faster. I mean they do have to do it, so it doesn't fall down. And we do have to turn around these assets we're getting back. It's just the nature of the business.

Gabriel J. Poggi
Raymond James & Associates, Inc., Research Division

Only quick follow-up to that would be is, I have to imagine and you alluded to it, Barry. Buying back stock has got to be at the top of the 'best investments you can make' list right now with the implication that loan book...

Barry Stuart Sternlicht
Chairman & CEO

What are we authorized to buy back? $400 million. We're well aware of it, and we had to be out of the market because we knew what our earnings were. But as of this moment, we can go back in the market. So we're on your side. Have a great summer, the rest of it, and we'll see you in the fall. Bye-bye.

Operator
Ladies and gentlemen, thank you for your participation. This does conclude today's teleconference. Please disconnect your lines, and have a wonderful day.