

Starwood Property Trust

First Quarter 2026 Earnings Call Transcript
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Presentation

Operator

Greetings, and welcome to the Starwood Property Trust First Quarter 2026 Earnings Call. [Operator Instructions]. It is now my pleasure to introduce your host, Zach Tanenbaum, Head of Investor Relations. Thank you. You may begin.

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 results 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 am 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. Today, we reported distributable earnings of \$147 million or \$0.39 per share for the first quarter. Our results were impacted by continued higher-than-normal cash balances, the resolution of nonperforming assets and the ongoing optimization of our new Net Lease cylinder, adjusted for which DE would have been \$0.47. I will provide more detail for these items within my business segment discussion.

As we continue on our stated path to grow our investment base, resolve our nonperforming assets and optimize our new Net Lease platform, our underlying earnings power continues to build. In the quarter, we deployed \$2.5 billion of capital across our businesses, including \$1.5 billion in Commercial Lending, \$597 million in Infrastructure Lending and \$128 million in Net Lease, bringing total undepreciated assets to a record \$31.7 billion at quarter end. We deployed another \$1.5 billion after the quarter, 70% of which was in commercial lending. Our company is diverse with Commercial Lending comprising just 52% of our investment base and owned property increasing to 25% this quarter. We are really not a typical mortgage REIT.

I will now take you through our individual segment results, beginning with Commercial and Residential Lending, which contributed DE of \$172 million to the quarter or \$0.45 per share. In Commercial Lending, we funded \$894 million of our \$1.5 billion in loan originations, along with another \$278 million of pre-existing loan commitments. After factoring in repayments of \$835 million, our funded loan portfolio grew to \$16.7 billion. This does not include \$1 billion of new originations after quarter end which brings our loan portfolio to its highest level since inception or \$2.3 billion of unfunded commitments on previously closed loans that will generate future earnings when funded.

I mentioned earlier that our run rate earnings were impacted by our resolution of nonperforming assets. During the quarter, we sold a multifamily asset in Conyers, Georgia that was foreclosed in February of last year. We've repositioned the asset during our 1-year hold period, cutting delinquency in half from 16% to 8% and increasing occupancy from 86% to 91%. After a broad marketing campaign in over 20 qualified bids, we sold the asset for a \$5 million DE loss and a small GAAP gain, reflecting the adequacy of the GAAP reserves we previously recorded on this asset.

We foreclosed on 3 5-rated nonaccrual loans in the quarter, the first of which was a \$248 million mixed-use property in Dallas, consisting equally of multifamily and hospitality; the second was a \$71 million multifamily in Phoenix; and the third was a \$28 million multifamily in Dallas. We obtained independent third-party appraisals for all 3 assets with the mixed-use property that represented 2/3 of this quarter's foreclosures appraising 10% above our basis. The other 2 assets carried a combined \$25 million of specific CECL reserves.

The weighted average risk rating on our loan portfolio improved to 2.9 this quarter versus last quarter's 3.0. This improvement is net of 2 small multifamily loans that were downgraded from a 3 to a 4 in the quarter, which Jeff will discuss.

We ended the quarter with \$676 million of reserves, \$455 million in CECL and \$221 million in REO. Together, these translate to \$1.82 per share book value, which is reflected in today's undepreciated book value of \$18.97.

Turning to residential lending. Our on-balance sheet loan portfolio ended the quarter at \$2.2 billion, down from \$2.3 billion last quarter due to repayments of \$38 million and a \$21 million negative mark-to-market adjustment on the portfolio that was offset by the \$31 million positive mark-to-market we recorded last quarter. Our retained RMBS portfolio remained relatively steady at \$400 million.

Next is Infrastructure Lending, which contributed DE of \$22 million or \$0.06 per share to the quarter. Our strong investing pace continued with \$597 million of new loan commitments of which \$567 million was funded. After factoring in repayments of \$320 million, our portfolio increased to a record \$3.2 billion. Nearly 70% of this quarter's commitments were self-originated, bringing our total self-origination volume to \$950 million.

Also in the quarter, we completed our seventh actively managed infrastructure CLO, a \$600 million transaction at a record low spread of SOFR plus 1.68%. We used a portion of the proceeds to repay CLO-3 for \$330 million. CLOs now represent 75% of our infrastructure debt, providing a durable, nonrecourse, non-mark-to-market financing.

Turning to our Property segment. We recognized \$29 million of DE or \$0.08 per share across all 3 major portfolios. I will start with a brief comment on our Florida affordable multifamily portfolio, Woodstar. Last week, HUD released the new maximum level LIHTC rent levels, which were set 8.9% higher than last year. Certain properties were in geographies where the rent increases were once again capped by HUD with the incremental rent growth being deferred to next year.

To date, we have recouped 100% of our original equity investment in this portfolio plus an incremental \$540 million that we have been able to reinvest across our business lines. We have \$416 million of Woodstar debt maturing in Q4 and anticipate another cash-out refinancing, again affirming our valuation on these assets.

In Net Lease, as I mentioned earlier, we are still in the ramp-up phase of this business, which has been quite dilutive following our acquisition 8 months ago, a dynamic we anticipated and disclosed at the time. If optimized and at scale, this business would have contributed \$0.03 of incremental DE to the quarter. The quarter's acquisition volume was in line with our original underwriting, with \$128 million of purchases containing a weighted average lease term of 19.5 years and weighted average rent escalations of 2.5%, bringing our total portfolio at quarter end to \$2.5 billion with a weighted average remaining lease term of 17.4 years and 0 defaults. As you are aware, we adjust DE for the straight-line rental income reflected in our GAAP numbers. If we were to include straight-line rent in DE, it would add another \$0.01 to the quarter.

We continue to optimize this platform's capital structure, completing 2 notable refinancing since our last earnings call. The first is a new ABS transaction, which was used to replace a more costly issuance that we assumed in connection with the acquisition. The ABS financing totaled \$466 million at a weighted average fixed rate of 5.06%, a record tight spread for this platform. This allowed us to replace \$324 million of existing ABS financing, which carried a weighted average fixed rate of 6.65%. The impact on our master trust was a reduction of 44 basis points from 5.73% to 5.29%, a benefit that we will realize in DE over time. However, during the quarter, we recognized a \$0.01 nonrecurring DE loss as a result of unwinding the interest rate hedges we had put in place in anticipation of this securitization.

The second refinancing was completed after quarter end with the closing of a new 5-year \$1 billion warehouse facility. It has a 40% lower spread and is nearly twice the size of the in-place financing we assumed to add acquisition. These accretive financings, combined with the ramp in transaction volume, builds the foundation for the earnings power embedded in this platform and paves the way to overcoming the \$0.03 of dilution that we recognized this quarter.

Concluding my business segment discussion is our Investing and Servicing segment. Collectively, the cylinders in this segment contributed a robust DE of \$57 million or \$0.15 per share to the quarter.

Our special servicer, LNR, continues to perform as the positive carry credit hedge we have long described with servicing fees increasing to \$52 million this quarter. Our active servicing portfolio totaled \$9.9 billion, while our named servicing portfolio was \$95 billion. LNR continues to be the highest rated special servicer in the country with a rating of CSS-1, the highest rating possible.

Our conduit, Starwood Mortgage Capital, securitized or priced \$153 million of conduit loans in 3 transactions at profit margins that were at or above historic levels. We typically see lower securitization volume in Q1 and expect to see volumes increase in the near term.

Turning to liquidity and capitalization, our current liquidity stands at \$1 billion, which does not include liquidity that could be generated from cash out refinancings, sales of assets in our Property segment, direct leveraging or issuing corporate unsecured debt backed by our unencumbered assets, or issuing Term Loan B, where we have nearly \$1 billion of capacity today. In addition, we have \$9.4 billion of availability across our bank financing lines. We continue to operate at conservative leverage levels, ending the quarter with a debt to undepreciated equity ratio of 2.59x.

Also notable this quarter, our Board authorized a \$400 million share repurchase program on February 26. In March, we deployed the first \$20 million of that program purchasing 1.1 million shares at a weighted average price of \$17.67, a discount to both our current stock price and undepreciated book value per share.

And one final note. During the quarter, we are proud to have been awarded the 2025 Mortgage REIT of the Year by PERE credit. The award reflects the breadth and resilience of our diversified platform across market cycles. With that, I will now turn the call over to Jeff.

Jeffrey F. DiModica
President

Thanks, Rina, and good morning, everyone. Let me start with the broader backdrop because it's important context for the quarter. Capital markets have been volatile to start the year, driven largely by geopolitical developments in the Middle East. Treasury yields and credit spreads have moved with each headline, and while volatility has increased, the overall environment remains relatively stable.

Refinancing volumes are significantly elevated with loans originated before the 2022 rate rise facing their final extensions and newer vintage loans coming out of call protection and taking advantage of spreads that are today at the tight end of their long-term ranges. This backdrop is constructive for our legacy investments and leaves us well positioned to capitalize on new origination opportunities at scale. Starwood Property Trust is a differentiated multi-cylinder platform that was built to outperform in volatile market environments, spanning commercial, residential and infrastructure lending, owned real estate and special servicing. This diversification gives us the earnings profile of a credit business with the upside from our large-owned property portfolio, our countercyclical special servicer, early prepayment income and further resolutions in our lending book.

We have invested in every quarter of our 17-year history. And when we see outsized opportunities like we have over the past year, we have the firepower to lean in, we've done just that with nearly \$4 billion of investments closed year-to-date. We are expecting a very robust finish to the first half of the year with an equally strong pipeline extending into the second half.

From a portfolio standpoint, we continue to see the benefit of repositioning we began several years ago. Multifamily and Industrial continue to dominate our pipeline, and we continue to grow our non-U.S. Loan portfolio, where our manager, Starwood Capital, has large originations team spanning the globe with decades of lending experience. Starwood Capital is also one of the largest private data center owners in the world with over 150 dedicated people in the sector, giving us the expertise to also make loans on data centers with confidence. Their footprint also allowed us to be a first mover lending in this space, taking advantage of wider spreads on loans that generally have 15- to 20-year leases to investment-grade tenants and fully amortized over the initial lease term.

U.S. office represents 7.6% of our assets today, which is well below our peers and represents the bulk of our reserves. Additionally, we only have one life science loan for \$56 million. And together, these sectors are less than 8% of our assets, which is extremely low in our industry and allows us to have more certainty regarding potential portfolio outcomes.

As Rina mentioned, our overall risk rating fell from 3.0 to 2.9 in the quarter. I will note that nearly half of the over 50 loans in our history that have been risk rated 4 or 5 have now been resolved or returned to a 3 or lower rating. Also, over half of our CRE lending commitments have been originated since 2024 at a lower basis and with better loan coverage metrics. We still have work to do, but we have meaningfully repositioned the portfolio in this cycle, leaving us in a good position relative to where the market is today.

Our approach to credit remains consistent. We lean into situations where we have conviction and control, and we are willing to use our balance sheet and large internal asset management resources to actively manage outcomes rather than fire sale assets at a worse outcome to shareholders. We have a proven track record of successfully stepping in when sponsors stop supporting and investing in assets. Along with our Manager, we have the willingness and proven operational capability in-house to improve performance and protect and potentially grow value.

We continue to make steady progress resolving legacy assets. Nonaccrual and REO balances declined again this quarter, and we have now resolved over \$300 million of assets that were previously a drag on earnings. We have additional REO sales in process and expect further reductions in the remainder of the year and in 2027.

We did see some ratings migration in this quarter, which is consistent with where we are in the cycle. Two loans moved into the 4-rated category, both in multifamily. The first is an \$81 million multifamily asset in Georgia, where the current debt yield is tracking below the extension threshold required at the upcoming maturity. The second is a \$40 million multifamily asset in Texas, where the sponsor has signaled an unwillingness to continue supporting the asset. Both situations are ones we have navigated many times. We have defined action plans. Both are being actively monitored and we are prepared to step in and execute these plans should we need to.

Our 5-rated loan category declined by over \$200 million in the quarter, including the \$347 million Rina mentioned offset by our purchase of the \$114 million senior position on a large industrial asset proximate to Manhattan. We are working to resolve this asset and the sponsor has leases under negotiation for almost all of the available space. Successful resolution of this loan, our largest in the 5 risk category, would decrease our 5-rated bucket by over 50%. That progress along with continued growth in our investment balance represents the core pillars of management's plan to grow earnings and dividend coverage as we have outlined in prior quarters.

In Infrastructure, a business we are in our ninth year investing in, we committed \$597 million at above-trend returns in the quarter. A majority of that activity was self-originated, which allows us to dictate credit and structure while continuing to grow our portfolio and earn excess return given our ability to finance this business accretively.

These loans are also supported by durable long-term demand drivers from the energy transition and AI-driven power infrastructure build-out, leaving us with a pristine low LTV portfolio. Our financing is diverse, low spread and benefits from nonrecourse, non-mark-to-market provisions in our CLOs, which as Rina said, account for 75% of this segment's debt.

Our Net Lease platform, Fundamental Income, continues to ramp as per our acquisition plan. We expect volumes to increase throughout the year as the team completes their first year under Starwood Property Trust. As Rina mentioned, we again made meaningful progress on the financing side in the quarter. The combination of a lower cost of funds and a higher advance rate, which we underwrote and have now executed on is directly accretive to the ROE of the cylinder and demonstrates what Starwood's capital markets relationships help bring to this platform. These improvements should help turn this business accretive in 2027 in line with our underwriting, supporting our thesis of creating long-term shareholder value at the expense of short-term earnings dilution we have experienced to date.

Our REIS segment again performed very well. The servicing platform continues to act as a positive carry credit hedge, generating higher earnings during periods of stress. Since the rate rise, we feel the equity market has undervalued the countercyclical nature of this business on our stock, but it proved again this quarter, it is a real differentiated earnings contributor with our highest ROE.

I would now like to spend a few minutes discussing our low leverage balance sheet. We have been and plan to continue to tactically increase our unsecured debt as a percentage of our company's capital structure. Unencumbering assets to move to more stable, non-mark-to-market financing is supportive of our corporate credit ratings, which we hope to improve as we execute on this plan. Our unsecured debt continues to trade very well, which we view as a reflection of the debt market's confidence in our balance sheet and the value of the diversity of our platform.

Our next corporate unsecured maturity is \$400 million in July and we have multiple options to address it. We have ample liquidity to repay it with cash or refinance it to take advantage of the strong current credit market backdrop I started today's call describing. Our access to the debt capital markets is genuinely differentiated. There is no other company in our space with the same footprint across secured, unsecured and securitized funding channels.

Wrapping up, we're the oldest and largest mortgage REIT with an equity base that is larger than our next 4 peers combined and as much trading volume as those peers combined, giving shareholders unparalleled liquidity. In our 17 years, we have built a unique diversified business and invested almost \$120 billion of capital while successfully navigating multiple cycles, leaving us as the only mortgage REIT to have never cut our dividend. We have a clear path forward, continue to resolve legacy assets while scaling our investment platforms. Progress across each of these areas is tangible, which we expect to improve earnings and dividend coverage. With that, I will turn the call to Barry.

Barry Stuart Sternlicht
Chairman & CEO

Thanks, Jeff. Thanks, Rina. Thanks, Zach, and good morning, everyone. I apologize up front, I'm not feeling well. So doing this with half a stomach. Wow, it's an interesting world. I think you'd like to say that there's never been so excited and so terrified at the same time. And it's not just the war. Obviously, it's what is the impact of AI long term on the markets, the office markets, the employment base, what would the politicians do, in the face of potentially job losses, what will happen with Taiwan, which the markets obviously think is a zero risk given the daily highs.

I tend to think the real estate sector, in general, is coming out of the frozen tundra of the last three years. We're still recovering from the 500 basis point increase in rates. And almost no one saw it coming and then the slow descent even though ex rents, inflation had clearly descended.

If you think about the world, it's sort of an odd concept. I was in a room of a lot of people out West recently, and I asked people to raise their hands, how many people would have expected what's going on in the world, the war, oil prices, deglobalization, trade wars, how many people would expect the stock market to be at all-time highs?

And it's sort of a strange thing. But in the middle of this, the real estate markets are curing themselves, although it's slow and it's not quarter-to-quarter. Supply is dropping dramatically in multifamily, supply is dropping in industrial, supply is stagnant, almost nonexistent in the office market, same in retail, senior housing. All these sectors are benefiting from capital being sucked into other things, including data centers, which is an asset class we play on both the equity and the debt side. We're just moving beyond, of course, with the risk of Taiwan, shutting it all down, ending the party. I'm sure the Chinese know.

So when it comes to us, I mean we sit here as a unique company with diversified asset business lines. We keep adding new business lines. We have quite a few assets that are not earning a fair return, whether REO or whether nonaccrual loans. When you look at our stock, you're earning from about 75%, something like that of our asset base. It's not our full asset base. It's almost like valuing a company that has a major tower under construction and on the balance sheet, it shows up in the work in progress, not as an asset, but when it's completed, it will produce earnings.

I think it's the same story today. We earned \$0.39 for the quarter, not a number we're happy with. If you back out the dilution, which will go away over time in Fundamental and triple net lease business, it'd be [\$0.41, \$0.42]. We have about 1.5 points drag of what we took in the quarter just hits to our earnings from the REOs. And some of those REOs when fixed up, we expect to actually make money on, but it takes time. We have a property that the developer will lose several hundred million dollars, we'll take it back. And we expect to be able to lease the whole thing and hopefully sell it at a gain.

And those are the kinds of opportunities, but they're not quarter-to-quarter. But with that confidence, we stepped up and bought stock in the quarter. We actually can't buy stock when we go into the blackout period, so that stops several weeks before earnings. And we'll continue to repurchase stock because it's a pretty good investment for us. Some of our businesses are really spectacular at the moment, and they're masking some of the noise of the less than spectacular parts.

The special servicer is cranking. Amazing this far along in the cycle. We still have \$100 billion of named servicing, and almost -- I think it's \$8.5 billion in named active in the servicing book. It's not going to be going down. That there is still a lot of distress. Rates are still higher. I should have mentioned when I talked to you about what we should think of the world, the 10-year hovering around 4.40%, 4.36%, 4.32%, 4.42%. I mean that's materially higher than I think most people would think. We're creating unprecedented deficits, but the equity markets don't seem to care very much.

Again, finishing the thought this is all good for real estate. The tide has gone out and the tide is turning, we're going from headwinds to tailwinds. And there are really two things behind the tailwinds, three really. One, the reshoring in the United States, bringing back all of these plant equipment, creating demand for industrial. That's a real trend. It's starting. It's not a massive tidal wave, but you're beginning to see the impact a little bit; two, supply, which we talked about; and three, interest rates because the forward curve is still lower.

And the markets are very confused as most executives are about a world -- I think post-World War II record low consumer confidence, but retail spending continues up. And I tend to think the post the GDP numbers are sort of the illusory. You can talk about them as being great and they are what they are, but they're really driven by two things, AI spending, which isn't felt by the average American and by productivity gains. And that kind of GDP is not the kind of GDP that normally would send those consumers to the store. And as you know, consumption is 70% of GDP.

So it is a miraculous economy, but it's not your grandma's economy, and it's creating all kinds of odd things and investors chasing multiples of revenues in the equity markets. So I think we will catch a bid. I mean, the entire real estate sector. And I can say that we've recently completed or about to complete our 13th fundraise of a fund on the equity side and robust investor demand where a year ago, they wouldn't talk to us. That's really a reflection of the turn in the markets and several of my peers in the asset management business have harped on their recent earnings calls, and we tend to agree things will be getting better.

The pace of our originations is solid. We're all looking for the earnings to come out of the book. We're confident in the ability to pay the dividend. We sit on \$1.5 billion of gains in our multifamily book. We actually made \$0.05 selling one asset, just one asset last quarter. So, quarter-to-quarter, we're sequentially up \$0.37 to \$0.39, but we chose not to take any of those gains. We're playing long ball, not short ball, and we're confident in our ability to create a dynamic company that's capable of producing superior earnings and therefore, dividends. And I want to thank the team that continues to work really hard to continue to lead the market in our field. Thank you.

Question and Answer

Operator

[Operator Instructions]

Our first question comes from the line of Jade Rahmani with KBW.

Jason Sabshon

Keefe, Bruyette, & Woods, Inc., Research Division

This is Jason Sabshon for Jade. It would be helpful to hear your thoughts on the outlook for resolving nonaccruals and foreclosed assets. Maybe comment on the time horizon and if possible, give a percentage range for resolutions in 2026 and 2027?

Jeffrey F. DiModica

President

Yes. Thanks so much. I appreciate the question. We, think we've told you we've resolved over \$300 million. We have a resolution that you'll see as an upgrade on a lease that was signed for about \$100 million in the quarter in Brooklyn. That will take an asset that now through three large leases has completely moved from a troubled risk rating of 4 or 5 back into something lower. We are expecting potentially a lease, as I spoke about on another asset just outside Manhattan where should we sign that lease, that will go from a 5 or 4. I think I mentioned in the script that 25 of the 53 loans we've ever had at the 4 or 5 have now been either worked out or moved back down.

Our strategy is just different than other people a bit on these. A lot of people are willing to do fire sale to a higher cost of capital buyer potentially with financing when they have a difficult asset. We look at every loan on a present value of the likely outcome to us. And given our access to liquidity, we have chosen to lean in. Rina gave you some examples in the quarter of even the multi that we lost, \$5 million or so on, we increased occupancy significantly, decreased the delinquencies significantly in the six months or so that we managed that property being managed by Starwood Capital. We have people with expertise in these.

So we're not afraid to take something back. We're not afraid to say, and we don't stay in for the sake of staying in. But if the present value of getting the money back today versus investing in the asset, if the present value is higher on the latter, we'll do the latter. So we have a few that you'll see play out. It will put us over \$500 million or so, I think, in the very near future. We're expecting \$900 million by the end of the year in our plan and then another \$500-or-so million next year in our base plan that will work most of the way through it. But it's very difficult to judge when you will get a lease and when something will play out and when the present value calculus for us will turn positive versus negative on making our decisions.

Jason Sabshon

Keefe, Bruyette, & Woods, Inc., Research Division

Great. Very helpful. And then separately, it'd be helpful to touch on the outlook for Net Lease and when you'd expect it to become accretive? I know you guys cited \$0.03 of dilution, but you also issued ABS and entered into a new credit facility. So any commentary there would be helpful?

Jeffrey F. DiModica

President

Yes. Thanks so much. This is an interesting one. We signed on -- you all know we weren't earning the core dividend at the time we closed this deal in July of last year. We made a decision knowing -- this business is running exactly at what

we expected it to run in the short run. We knew we had to optimize the financing. We knew we would get originations up. We made a decision to take on negative DE for up to six quarters. I think when we did it, we told people it would become accretive in '27.

And so it's not often that a company like us takes six quarters of negative DE at a time where we're not earning the dividend. But we did that because we wanted to own this platform. We were buying a platform that we knew would be short-term dilutive. And as you look at the rent bumps over a number of years, it becomes very accretive down the line. So as large shareholders with management and our Board, we looked at the long term here. We are obviously paying a penalty for it in the market today because missing a number as you see in today's stock price is not something that bots like very much, but we set this up for the long term. We think the business will perform. It's -- as you said, we've now optimized the financing, which starts kicking in and will help it turn to be accretive in '27. It becomes very accretive beyond that. But I'll turn it to Barry for any other comments that he might have.

Barry Stuart Sternlicht
Chairman & CEO

Well, a couple of things. One, the fundamental business, if it traded separately, we probably trade at a 5% or 6% dividend yields, and it's tucked into us. And obviously, it's hurting us when in fact, it's probably a significant value as a stand-alone business, which isn't lost on us. So one way or another, we're going to get this thing to scale or spin it out or do something that will create, I reflect the value in the business. It is -- we're not using straight-line accounting on their leases. Some of our peers do that. With that, I mean our yields would be significantly higher even this year.

So zero defaults, 100% occupied portfolio, growing at about the pace -- I'd say it's going at the pace we underwrote, but not nearly as fast as I have hoped. So -- and that's one of the reasons you see the dilution. But I think you have to look at just answering the former question. We're going to work as fast as we can to repair these nonaccrual assets and the REO assets. But as Jeff mentioned, we don't have the need to give them away. At the end of the day we're real estate guys.

And so if we can -- what you see in most of these assets, especially the ones that get in trouble is the borrower just stopped taking care of them, right? So you have a multi that has rooms out of service because he just didn't care because he was going to lose the asset or you have tenants that won't take on an office asset because the borrower has no desire or any need to put in tenant improvement dollars. He's just flushing his cash.

So you get these in some cases, really good assets that have been abandoned by the borrowers. It takes time to actually get them back to stabilization and then you sell them. It's not -- sadly, it'd be easier if this was a closed-end fund kind of thing. And it's not done to optimize earnings quarter-to-quarter, it's done really to maximize return on the capital that we've invested behind these properties.

So -- and we are blessed with a fortress balance sheet so we can put the money into convert as we are doing on K street in D.C., which is being converted from an office building to a rental. And in the time that we've taken the underwriting rents have gone up. So our yields on cost would be even better than we thought and expect they will be. It didn't seem to fire half of D.C.

So when we complete that, but that's not going to get done for another year or year and a half. And it's -- so that's the kind of situation. I mean, we're confident. We're major shareholders of our stock. As you saw, we repurchased stock. So we're confident in our ability to weather the storm and continue to pay the dividend and wait for cleaner numbers, frankly. The base isn't bad. It's just not very clean. So we know all that.

Operator

[Operator Instructions]

Our next question comes from the line of Gabe Poggi with Raymond James.

Gabriel J. Poggi

Raymond James & Associates, Inc., Research Division

Kind of piggyback on the last question. If \$0.48 of the dividend coverage is the goal, help us or me shape kind of where we are in that timeline based on these first quarter results. I know Barry just said there's a lot of noise in it and the dilution from net lease, et cetera. But how should we think about kind of the timetable to get to \$0.48 as you guys are working through nonaccruals, as you're taking time with REO and being patient, et cetera, et cetera? That's question one.

Rina Paniry

CFO, Treasurer, Principal Financial Officer & Chief Accounting Officer

Gabe, thanks for the question. So as I mentioned in my remarks, I think we're there on a recurring basis today, right? We're not there on a reported basis. So we need to work through. We talked about Fundamental. And we think that, that becomes breakeven, call it, early next year and then accretive thereafter. So we think on a recurring basis, we would be in excess of the dividend at some point, probably late next year. We had higher-than-normal cash balances that we talked about last quarter. We raised excess financing on our Woodstar Refi, we had two debt raises.

So we're still fighting the cash drag from having over \$1 billion of cash for the quarter. So we need to get the money deployed, and I think that will help. But I would say you're not going to see kind of above on a recurring basis until next year at some point. And we still have to work through the REO assets.

Jeffrey F. DiModica

President

That's right. We've been saying that consistently though, Gabe, for a while that end of '26 as we get into 27, that's what we're hoping. There are a little nuances along the way. You talked about cash drag. We don't tend to whine about the timing of cash flow. But in this quarter of the \$1 billion or so of CRE loans, 57% of them were funded, which means 43% weren't. On average, they're only funded for 27 days on that 57%. So we're getting very little credit there versus in the quarter, our repayments were outstanding for 64 days. That probably cost us \$0.01 or \$0.02 as well.

They are just small nuances. But I think if you normalize fundamentally, you go into the upside that Rina talked about and the other businesses, we start to get down as per the plan, I just told you on nonaccruals, et cetera., and we continue to originate at this very elevated pace with great quality originations. We're really proud of the book that we're building over the last couple of years, half of which is 2024 and beyond originations. It will all come together as we turn the year to getting to that \$0.48 that actually is reported in the bots like more than today's.

Barry Stuart Sternlicht

Chairman & CEO

I'm going to be more optimistic than Rina and Jeff because I know about some situations that we will trigger. And if we have to sell some assets to be able to redeploy the capital at the 11%, 12%, 13% ROEs, then we'll do it. So I think there are some loans that are toggling to becoming accrual again, they're material. And I'd expect at least one of them to have a resolution in the next -- certainly, by the end of this year. And with that, there might be a -- it's a material earnings mover for us.

So I do think it's unacceptable to have \$0.11 or so or \$0.12 of dilution from Fundamental. So that's not a stable situation. If it doesn't get better, we're going to put it in its rightful home, which may not be here. So it's not acceptable, even though the businesses are performing well, the noise is too much for shareholders to come through. We could invite you into the house and show you our assets and you see the values are all there and our ability to earn the dividend and exceed it is certainly in the house.

It's just -- we told you about this last quarter. It's going to be a rocky road to get there, the values of assets. It's a puzzle and we've got to manage it in the best way to maximize returns to the shareholders. We are, as I said, large shareholders. So very motivated to do the right thing.

Jeffrey F. DiModica
President

Getting back to the \$0.48, obviously, would be the holy grail is the only thing that we did with CRE lending. That's 52% of our business. We have \$1.3 billion of gains, Gabe, away from this. We've always had recurring, nonrecurring gains that come from things. The servicer had a good quarter this quarter. SMC often has a good quarter. It was light this quarter. We used to get a lot of prepaid penalties. Those are coming back in this tighter spread environment. We're going to start getting prepay penalties again.

All these recurring, nonrecurring things, will get us over that number. Never mind the fact we have \$1.4 billion of gains sitting outside of it. I think the construct to hold somebody to earning it all in the core business or you take the stock down significantly, doesn't really apply as much to a well-diversified company that's always had recurring nonrecurring gains, and we will have recurring nonrecurring gains through the rest of this year.

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

That's all very helpful color, especially on the timing stuff, Jeff, and I fully appreciate that it takes time to work through this. Follow-up, Jeff, you had mentioned that you guys -- that there was some REO kind of potentially in the sales process or beginning to kind of kick that ball down the road. Is there any more color you can give on that as it pertains to -- you took some keys this past quarter, just kind of what we're looking like potentially, and Barry just alluded to that, where some of those sales -- those sales could be pulled forward to reallocate capital?

Jeffrey F. DiModica
President

Yes. We will -- we prefer to let you know when they happen because the market's moved pretty quickly. There are two or three that we think happen fairly soon. There are a couple of leases that could move to nonaccruals. Away from nonaccrual, I think you'll see that with some potential upgrade. But I don't want to signal any of the sales quite yet, Gabe. But I gave you the sense that we hope to get through \$900 million this year and \$500 million next year off that list, and that will be a combination of a number of things, but nothing imminent that we're going to report here looking forward.

Barry Stuart Sternlicht
Chairman & CEO

Thank you, everyone, for joining us, and we'll see you again next quarter.

Operator

Ladies and gentlemen, this concludes today's conference, and you may disconnect your lines at this time. We thank you for your participation.