Granite Point Mortgage Trust Inc
Third Quarter 2024 Earnings
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Presenters
Jack Taylor, CEO
Marcin Urbaszek, CFO
Stephen Alpart, CIO
Peter Morral, Chief Development Officer and Co-Head of Originations
Steve Plust, Chief Operating Officer
Blake Johnson, Deputy CFO
Chris Petta, Investor Relations

Q&A Participants
Steve Delaney - Citizens JMP
Doug Harter - UBS
Jade Rahmani - KBW

Operator
Good morning. My name is Christine, and I will be your conference facilitator. At this time, I would like to welcome everyone to Granite Point Mortgage Trust's Third Quarter 2024 Financial Results Conference Call. All participants will be on a listen-only mode. After the speaker's remarks, there will be a question and answer period. Please note, today's call is being recorded. I would now like to turn the call over to Chris Petta with Investor Relations for Granite Point.

Chris Petta
Thank you and good morning, everyone. Thank you for joining our call to discuss Granite Point's third quarter 2024 financial results. With me on the call this morning are Jack Taylor, our President and Chief Executive Officer; Marcin Urbaszek, our Chief Financial Officer; Steve Alpart, our Chief Investment Officer and Co-Head of Originations; Peter Morral, Chief Development Officer and Co-Head of Originations; Steve Plust, our Chief Operating Officer; and Blake Johnson, our Deputy Chief Financial Officer.

After my introductory comments, Jack will provide a brief recap of market conditions and review our current business activities, Steve Alpart will discuss our portfolio, and Marcin will highlight key items from our financial results and capitalization. The press release, financial tables and earnings supplemental associated with today's call were filed yesterday with the SEC and are available in the Investor Relations section of our website, along with our Form 10-Q.

I would like to remind you that remarks made by management during this call and the supporting slides may include forward-looking statements, which are uncertain and outside of the company's control. Forward-looking statements reflect our views regarding future events and are subject to uncertainties that could cause actual results to differ materially from expectations. Please see our filings with the SEC for a discussion of some of the risks that could affect results. We do not undertake any obligations to update any forward-looking statements.

We will also refer to certain non-GAAP measures on this call. This information is not intended to be considered in isolation nor as a substitute for the financial information presented in accordance with GAAP. A reconciliation of these non-GAAP financial measures to the most comparable GAAP measures can be found in our earnings release and slides, which are available on our website.

I will now turn the call over to Jack.

Jack Taylor
Thank you, Chris, and good morning, everyone. We would like to welcome you and thank you for joining us for Granite Point's third quarter 2024 earnings call.

Before discussing our third quarter results, I'd like to take a moment to briefly discuss our upcoming CFO transition. As previously announced on December 1st, Marcin Urbaszek will depart Granite Point and Blake Johnson, who rejoined us early last month, will take over as CFO. Blake and Marcin have been hard at work with our team for the past month, ensuring a smooth transition. Having had the privilege to work closely with him since the inception of our business, I have come to admire Marcin greatly for his honesty, character, intelligence, and dedication. Marcin has left an indelible mark on our company, and we are grateful for his leadership and friendship. Marcin, you'll be missed and all of us at Granite Point wish you the very best in your next chapter.

At the same time, we are also very excited to have Blake back at Granite Point. Blake played an integral role in establishing our finance, accounting and tax functions, most recently serving as our controller. Both during that time and in the past month, I have seen firsthand Blake's financial expertise, industry acumen and leadership capabilities. I am confident that his deep understanding of our business and his extensive history with our team make Blake the perfect fit to advance our initiatives and drive shareholder returns as our next CFO.

Now turning to our business activities. The third quarter marked a period of substantial progress for Granite Point, driven by our proactive approach to resolving nonperforming loans and generally improving real estate market conditions. The Federal Reserve began its long-awaited interest rate cutting cycle, which, along with improving liquidity and the overall market sentiment, should be supportive of real estate valuations and transaction activity going forward.

We maintain our view that the commercial real estate market conditions in large part will be dependent on the forward path of interest rates, which remains somewhat uncertain, given the Fed's focus on the macroeconomic data that continues to point to the ongoing strength and resiliency of the broader economy. The CMBS market has grown significantly stronger during the year, especially for larger commercial mortgage loans. Liquidity in the floating rate transitional middle market sector, though improving, remains less robust, particularly as regional and community banks are largely on the sidelines. But this will present attractive longer-term opportunities for nonbank lenders to grow their market share over time.

So far this year through the third quarter end, we have resolved six loans totaling about $205 million and realized about $283 million of principal balance loan repayments and paydowns, including office loans, with most of this activity occurring during the third quarter. More importantly, we have maintained strong forward momentum for the rest of the year and beyond with a pipeline of over $280 million of loan resolutions across six assets, one of which closed in October at our carrying value and we expect most of the remainder to be completed during the fourth quarter or shortly thereafter.

We are adequately reserved for these loans and don't anticipate a material book value impact as they resolve. We are pursuing resolutions of our remaining 5-rated loans, most of which are in various stages of their respective processes and anticipate those transactions will be finalized through the first half of next year, though some may take a bit longer given their challenging local market dynamics. As we have addressed the credit issues within our portfolio, we have successfully executed on multiple different resolution strategies.

Our portfolio management approach emphasizes the balance between timing, potential profitability, book value impacts, liquidity needs, and other factors with the goal of optimizing the economic outcomes for the company and our various stakeholders over the long term. We anticipate our CECL reserve balance will decline significantly in the coming quarters, given the improving confidence in the commercial real estate market, a pickup in the transaction activity and our momentum on loan resolutions. We believe we have reached a point where the volume of nonperforming loan resolutions will meaningfully exceed any potential future credit events, although we may experience some idiosyncratic credit migration in the future.

We expect this ongoing turnover and repositioning of the portfolio to improve our run rate profitability over time, driven by multiple factors, including turning those loans into earning assets by providing seller financing, repaying expensive debt, reinvesting capital return from repayments, and remaining opportunistic with respect to our capital structure. To that point and consistent with our capital allocation strategy of assessing all opportunities and executing on the ones that are most attractive, during the third quarter, we repurchased an additional 700,000 common shares, reflecting our strong belief that our stock continues to be significantly undervalued.

Moreover, our board increased our repurchase authorization by an additional 3 million shares, bringing the total to about 5.9 million shares available for buybacks, which further increases our capital return strategy flexibility by allowing us to remain opportunistic with respect to any potential buybacks. We have made meaningful progress over the last few quarters, improving the overall credit profile of our portfolio through the resolutions of nonperforming loans. We believe our industry is getting closer to the end of this prolonged credit cycle and the period of extreme market stress and capital is gradually returning to the transitional lending space.

In the near term, we will remain focused on maintaining higher liquidity and proactively managing our portfolio. As we look towards the next couple of quarters and beyond, driving further turnover of our portfolio through resolutions and loan repayments will position us to return to our core lending business and take advantage of what we believe will be attractive investment opportunities in the future, growing our portfolio while improving our run rate profitability and driving attractive total shareholder returns.

I would now like to turn the call over to Steve Alpart to discuss our portfolio activities in more detail.

Stephen Alpart
Thank you, Jack, and thank you all for joining our call this morning.

We ended the third quarter with total loan portfolio commitments of $2.5 billion and an outstanding principal balance of about $2.3 billion, with about $109 million of future fundings, which accounts for only about 4% of total commitments. Our loan portfolio remains well diversified across regions and property types and includes 62 loan investments with an average size of about $38 million and a weighted average LTV of 64% at origination. Our realized loan portfolio yield for the third quarter was about 7% net of the impact of the nonaccrual loans, which we estimate to be about 210 basis points. During the quarter, we funded about $10 million of existing loan commitments and upsizes and realized about $285 million of principal balance in loan repayments, paydowns, and resolutions.

So far in the fourth quarter, we have funded about $4 million of existing loan commitments and realized a $33 million loan resolution. Given our emphasis on maintaining liquidity and resolving the nonperforming loans, we expect the loan portfolio balance to trend lower over the coming quarters before we begin reinvesting our capital, re-leveraging, and re-growing later this year.

We have been actively addressing the 5-rated loans in our portfolio and are happy to report significant tangible results and expect to resolve most of these assets over the next few quarters. During the quarter, we successfully resolved three nonaccrual loans totaling over $120 million in UPB through a variety of strategies. The mixed-use office and retail property securing our $37 million loan in Los Angeles was sold for cash by the sponsor. We restructured the $51 million loan secured by a mixed-use multifamily office and event-based property in Pittsburgh into a $32 million senior mortgage and a $19 million mezzanine loan with the sponsor investing additional capital into the property.

Additionally, the multifamily property located in Chicago, securing our $34 million loans was sold without us providing financing to the new owner. Through the third quarter, our resolutions totaled about $205 million of principal balance across six loans. So we feel very good about our progress to-date.

Now we'd like to provide some color on resolving the balance of our risk-rated "5" loans. In total, out of nine such loans we had at quarter end with a total UPB of about $509 million, one has been resolved and seven of the eight remaining are in active resolution processes. In October, the $33 million loan secured by an office property in New Jersey was resolved at our carrying value as of September 30th. During the quarter, we received an unsolicited offer to buy the loan on an all-cash basis with no staple or third-party financing in a quick close transaction, which we decided to opportunistically pursue. Given the pending resolution, the loan was downgraded to a risk rating of 5 at quarter end.

Going forward, we expect to resolve most of our remaining 5-rated loans through year-end 2024 and into early to mid-2025. We have over $280 million of resolutions across six assets that have either already closed or are expected to close in the next few months and anticipate one to two more to follow in the first half of next year. As we disclosed previously, the mixed-use office and retail property securing our $94 million loan in New York is under contract and the sale is anticipated to close during the fourth quarter. Additionally, in the coming months, we anticipate resolving the $81 million mixed-use loan in Baton Rouge, the $29 million hotel loan in Minneapolis, the $26 million office loan in Boston, and the $20 million office loan in Denver. In addition to the $280 million we just discussed, the sale process for the office property securing our $80 million loan in Chicago remains ongoing and may conclude in the first half of 2025. Given the persistent local office market challenges, we anticipate a longer resolution timeline for our $93 million loan in Minneapolis.

During the third quarter, we also downgraded to a risk rating of 5 our $53 million loan secured by a hotel located in Minneapolis. The collateral property is currently in the early stages of the sale process and the ultimate timing and outcome remains hard to predict.

Turning to our REO assets. We continue to pursue a potential sale for the Phoenix office property and that process remains ongoing. The office property in suburban Boston continues to perform well with a strong cash flow profile. After we took title, we extended the lease for the largest tenant and our current plan is to continue to operate a large portion of the property as office while also creating additional value through several redevelopment opportunities on the site. Both REO properties remain unlevered as of quarter end and serve as a source of additional liquidity, which we may access in the coming months to further optimize the balance sheet and increase our financial flexibility.

We have strong visibility for addressing most of our 5-rated loans. Market sentiment and transaction activity are improving. Debt and equity capital is available and looking to get invested and most of our strong and seasoned sponsors continue to support their assets. As a result, we are optimistic about the future of the business.

In the near-term, as we work through the remainder of our nonperforming assets, we intend to prioritize maintaining higher liquidity for more optionality to address any credit issues, which in turn will allow us to start reinvesting capital and begin originating new loans during 2025. I will now turn the call over to Marcin to discuss our financial results and our capitalization.

Marcin Urbaszek
Thank you, Steve, and thank you, Jack, for your kind words earlier. It has truly been an honor to serve as Granite Point's CFO since inception. It has been the highlight of my career and I've been very fortunate to work with an amazing and talented group of people along the way.

Now turning to our financial results. For the third quarter, we reported a GAAP net loss of $34.6 million or $0.69 per basic share, which includes a provision for credit losses of $28 million or $0.55 per basic share, mainly related to certain risk-rated "5" loans. Distributable loss for the quarter was $38 million or $0.75 per basic share, including write-offs of $44.6 million and an $8.8 million recovery of amounts previously written off. The write-offs were related to the three nonaccrual loan resolutions Steve discussed earlier.

Our book value at September 30 was $9.25 per common share, a decline of about $0.59 per share from Q2, which was mainly due to the loan loss provision mentioned earlier, partially offset by the accretive share buybacks we opportunistically executed during the quarter, which we estimate benefited book value by about $0.10 per common share.

Our aggregate CECL reserve at September 30 was about $259 million or $5.18 per share as compared to $267 million last quarter. The decline in our CECL reserve was mainly driven by the write-offs related to the resolutions, partially offset by an increase in the allowance on loans that were risk-rated "5," reflecting some additional pressure on property values.

Over 75% of our total allowance or $200 million is allocated to individually assessed loans, which implies an average estimated loss severity of about 39% on those assets. With the expected near-term nonaccrual resolutions Jack discussed earlier, we anticipate incurring over $120 million of realized losses over the next couple of quarters, the actual timing of which will depend on the closing of specific transactions. We believe we are appropriately reserved for these losses as of quarter end and the resolution should meaningfully reduce our total CECL reserve balance.

As of September 30, we had about $629 million of loans on nonaccrual status. Certain of these loans are in cost recovery and any incoming interest is applied to reduce loan principal rather than being recognized in earnings, which is estimated to be about $3.5 million in the third quarter.

We anticipate the run rate profitability of the company to improve as we continue to resolve nonearning assets, repay expensive debt, and reinvest our capital over time, though the exact timing and magnitude remain difficult to predict and will also be dependent on the volume of loan repayments and the level of short-term interest rates. Everything else being equal, we estimate that the $280 million of nonaccrual resolutions discussed earlier is expected to improve run rate earnings per share by about $0.05 to $0.06 per quarter.

Turning to liquidity and capitalization, we ended the quarter with about $113 million of unrestricted cash and total leverage modestly decreased to 2.2x in Q3 compared to 2.5x in Q2, mainly due to loan repayments and paydowns. During the quarter, we terminated the Goldman Sachs financing facility, which matured in mid-July as we anticipated limited use in the near term. We continue to enjoy strong support from our lenders, highlighting our long-standing relationships in the market, and we expect to expand our financing capacity once we return to originating new loans more actively.

As of a few days ago, we carried about $94 million in cash that we expect to increase in the coming weeks due to some loan repayments and the potential financing of our unlevered REO assets. And now I'd like to open the call for questions.

Operator
Thank you. We will now be conducting a question and answer session. If you would like to ask a question, please press "*" "1" on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press "*" "2" if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the "*" keys. One moment, please, while we poll for questions. Thank you. Our first question comes from the line of Steve Delaney with Citizens JMP. Please proceed with your question.

Steven Delaney
Good morning, everyone. Thanks for taking the question. Hey, look, congrats on the methodical process and working through this and I think you guys have been very clear that this is going to take time, but we understand the market and we applaud the thoughtful efforts you're putting in to resolve these assets.

Obviously, you gave us some time frame, these things are complicated. I know you can't be precise about that. But, Jack, based on what I'm hearing in terms of resolutions, would it be possible that you could become involved in new lending, say, the middle of next year? I guess what I'm trying to get at, Jack, you want to fix all your problem loans and you hope you don't have additional nonperformers coming on, but is the bar to have virtually no nonperforming loans before you start lending? Or is there a way to step into new loans because I understand there are attractive opportunities out there? So if you could just sort of respond to that about how we should think about the process and for the analysts here for modeling, when should we begin to project some sort of new loan originations to offset repays? Thank you.

Jack Taylor
Hi, Steve. Thank you. I'm happy you were able to join us today. So based on what we know today, we expect to return to our core lending business and start reinvesting capital during 2025. That

will be to take advantage of the attractive investment opportunities, which we think will be quite significant. The demand side is not very large yet from the borrowing community, but we expect that to grow significantly. And as we do that, we'll re-grow our portfolio.

Now we'll say that won't necessarily occur during the first quarter and we'll assess the timing as we get into the New Year based upon a variety of factors. And I'll point out, we have almost the entire originations and underwriting team intact from when we were doing $1.5 billion to $2 billion a year. And to answer your question a little more specifically, no, I don't think we have to resolve every asset because some of those can take longer. So I would expect that for your modeling purposes, you could think of mid-year, and we can try to be more precise as we move forward.

Steven Delaney
That's very helpful. Pretty much what I was hearing, but it's helpful to hear you express it that clearly. Your buyback has been built to, what, a little over between $15 million, $20 million, I guess, maybe $18 million. Stocks sitting here like at 30-some percent of book, I think. Should we expect that if the stock stays down here sub $5 versus your $10 book value, that there's going to be a continued steady utilization of that authorization?

Jack Taylor
Well, let me try to parse. I wouldn't say continued steady because that's a real prediction, if you will. But I will say that we continue to believe that our stock price represents a really strong value opportunity for the investors given the fundamental value of our business and the temporary market uncertainty, which we think we are all climbing out of. And a discount to book value is one of the main factors we take into consideration in assessing the best use of our capital. And so we try to balance that against other factors like liquidity, maintenance, and other things.

So while we don't really comment specifically on potential buybacks, I will point out that we think we're very cheap. We've been historically pretty active with respect to our buybacks. And over the last couple of years, we've bought back something like 5.8 million of our common shares in the open market and we'll continue to assess it in the context of what I just told you.

Steven Delaney
Thank you for the comments this morning. That's helpful.

Jack Taylor
Great. Thank you. Thank you for joining us.

Operator
Your next question comes from the line of Doug Harter with UBS. Please proceed with your question.

Douglas Harter
Thanks. You've made progress on resolving some of the nonaccruals, but they've kind of--others have kind of backfilled in. Can you give us how you're thinking about the current state of kind of the 3-rated loans or the 4-rated loans and your confidence that we won't see continued migrations down to 5?

Stephen Alpart
Hey, Doug. It's Steve Alpart. Thanks for joining. So I would say on the 4-rated loans, similar to the 5 we just discussed, we're focused on resolving all these loans in 2025 or as soon as possible. The 4-rated loans are generally office loans that are behind on business plan where I think everyone knows there's limited liquidity right now, although that is improving. We're working with all the sponsors on next steps.

We feel that the ratings we have, obviously, for the quarter are appropriate. That doesn't mean that there can't be further migration. We're hoping to resolve these loans or hopefully have some of them migrate to 3. It's possible that some could migrate to 5. But at this point, we think we've really identified the large majority of potential issues. But obviously, there's always upward and downward credit migration.

Douglas Harter
If you think about these migrations that have happened, kind of what happened this quarter that kind of led to the migration that kind of led to a worse performance than you had been thinking 3 months ago when those 4s were those new 5s or 4s? Just help us understand that.

Stephen Alpart
Sure. Well, there were 3 migrations--there were 3 resolutions during the quarter, the third quarter that were 5-rated loans. So those are loans that we had previously identified. We've been working on those for a while. We were happy to get those done. There was one migration that we resolved in the fourth quarter that did migrate. That was the one that we mentioned that we resolved during the fourth quarter.

That was a New Jersey office asset. We weren't necessarily looking to sell it, but that's the one that we referenced we were approached by someone who kind of opportunistically decided to pursue it. And that one was really as we kind of began to assess that asset during the quarter, we thought it was appropriate to migrate that one to a 5 and we were happy to get that one done in the fourth quarter.

Douglas Harter
Great. Thank you, Steve.

Stephen Alpart
Sure. Thank you, Doug.

Operator
As a reminder, if you would like to ask a question, press “*” “1” on your telephone keypad. Our next question comes from the line of Jade Rahmani with KBW. Please proceed with your question.

Jade Rahmani
Thank you very much. Just starting with the higher Treasury rates and what that might imply, do you think there'll be an impact on portfolio performance based on that?

Jack Taylor
Hi, Jade. Thank you for joining us and thank you for your question. I think not much. And what I mean by that is there's been an increase in transaction volume that has occurred because of rates coming down and some of the refis became more achievable and we've seen some of that in the regular way repayments.

But I would say that our deals that we have in process for resolution are not really dependent upon the tick-up in rates that have occurred. I do think that for the industry, with the election turning out as it did with the backup in the 10-year, there will be some pressure, I think pressure, but I think the general trend will continue to improve. But there will be some pressure on certain deals that were dependent upon a fixed rate takeout. But I don't think it's going to impact our portfolio because of the nature of the resolutions we're working on currently.

Jade Rahmani
Thank you. Appreciate that. Currently, there are about $1.095 billion of office loans in the portfolio of which $250 million are watch-list loans. So that implies about $840 million of remaining office loans and when I look at the portfolio duration, it's 1.4 years, which suggests clearly maturities will take place between now and year-end 2025. And we all know that's where the rubber meets the road at maturity date.

In office, what we're seeing from brokers is an uptick in office leasing activity. The problem is it's concentrated very much in Class A, highly amenitized new vintage buildings and everything else, which is the predominance of inventory, requires significant dollars to lease up in order to attract tenants. So this $840 million of remaining office loans risk-rated "3" or below, what is your viewpoint as to what happens when those maturities come up over the next 1.4 years?

Stephen Alpart
Hey, Jade. It's Steve Alpart. Thank you for joining. Great question. That's obviously a big focus of ours on our ongoing asset management. As we look out into the fourth quarter and out into 2025, and this comment is on all of the loans coming up for maturity, including the office, some of those are going to pay off in the normal course. Some of them are actually in process to pay off, including office, notwithstanding the challenges in the sector.

Some of them will extend as of right. Some of them will not pay off or extend as of right and we have a good playbook for working with those borrowers on a case-by-case basis. To the extent a borrower is committed to the asset, doing a good job, our playbook has been that in exchange for additional equity, which can take the form of a principal paydown, can be replenishing reserves, creating additional structure, we'll come up with a solution that we view as a win-win to buy more time. And we've had a limited number of cases where a borrower may decide that they don't want to put more equity in and we have a playbook for resolving those as well.

So the majority of these assets, the conversations are good. Borrowers are committed. The office assets need more time. Some will pay off, some will extend, some will modify. And again, as I said earlier, we think we've identified the majority of the problem assets, but we think we have a playbook for resolving this over time.

Jade Rahmani
Thank you very much.

Stephen Alpart
Thank you.

Operator
Thank you. Mr. Taylor, we have no further questions at this time. I would like to turn the floor back over to you for closing comments.

Jack Taylor
Thank you very much, operator. And I want to say to everybody that's with us on the call today, thank you for joining us. We really appreciate you taking the time. And again, thank you to Marcin and to Blake for such a smooth transition, and we wish you a very nice day. Thank you.

Operator
Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.