October 2023

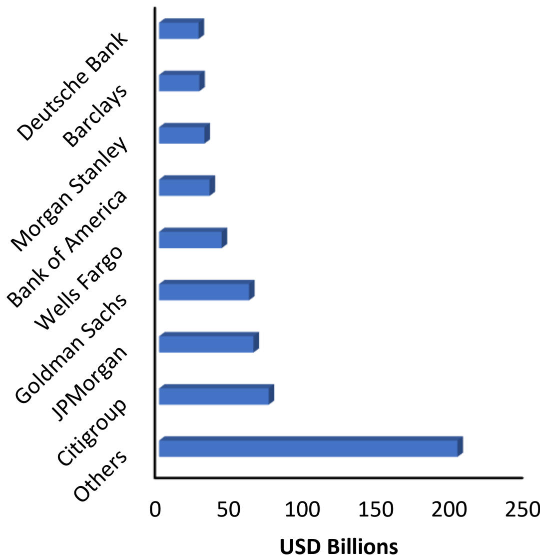
CMBS: Trends and Current Market Update

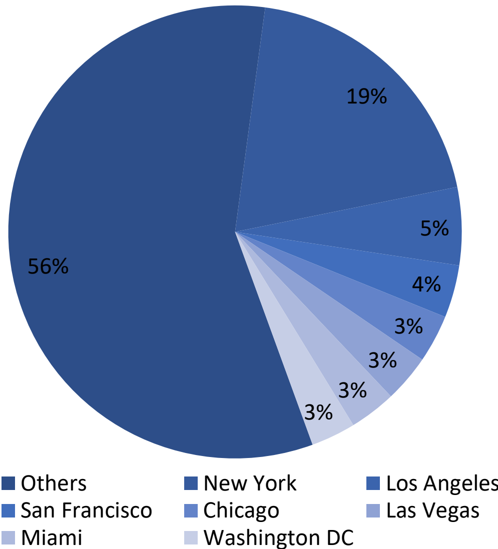
The commercial real estate market is moving against strong headwinds. Rising interest rates, weak demand for office and retail spaces, and investors' pivot towards safer investments amid economic uncertainty all seem to mount pressure on the market. Yet, it shows few cracks, so far at least. Delinquency rates remain low, and foreclosures are few and far between. Bent, but not broken, as some may say.

In this article, we take a deep dive into 1,729 private label CMBS deals issued from January 2013 to the present—many of which are set to mature starting this year, to provide an overview of what is out there and offer a glimpse into what may be coming.

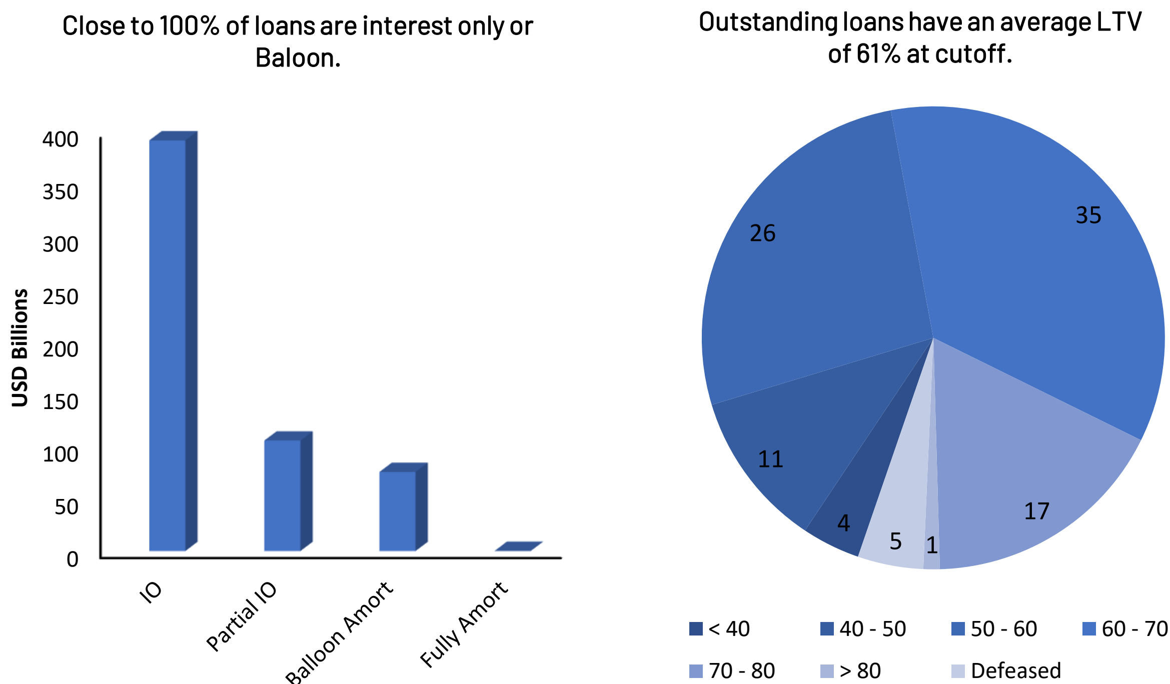
Outstanding CMBS Loans: A Quick Review

Our sample consists of 27,125 loans totaling $572 billion in balance at cutoff, supported by 77,974 commercial real estate properties. Citigroup, JP Morgan, Goldman Sachs, and Wells Fargo combined originated $242 billion of these loans. Nearly one-third of the outstanding balance is backed by properties located in just three MSAs: New York, Los Angeles, and San Francisco.





As is typical, nearly all loans in our sample are interest-only or balloon. On average, loans have a loan-to-value (LTV) ratio of 61 percent at cutoff, which is conducive to strong credit rating.[1] Worthy of note, however, is that as much as 18 percent of the loans are highly leveraged (LTV > 70%).



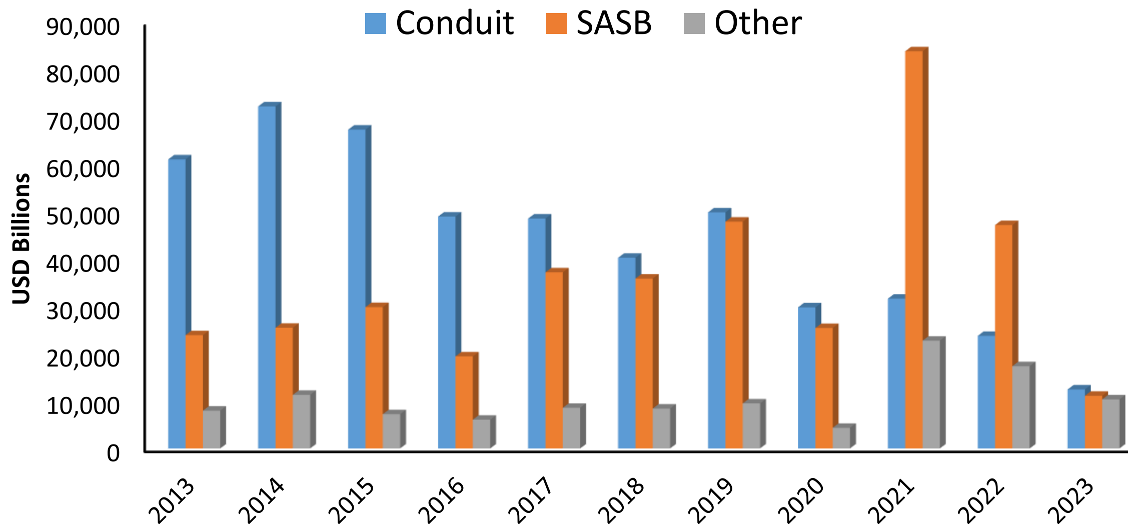
SASB Outpaced Conduit

Over the past decade, one of the most notable trends is the continued shift towards single-asset-single-borrower ("SASB") deals. As **Figure 1** shows, annual issuance of SASB deals nearly quadrupled from 2013 to a peak of $83 billion in 2021. Deals backed by conduit loans, the more conventional type of CMBS loans, have lagged behind.

Generally speaking, conduit deals are supported by multiple properties and many different borrowers. In contract, SASB transactions are instead backed by a single asset or a pool of cross-collateralized/cross-defaulted mortgage obligations by a single borrower. SASB deals are therefore less diversified and potentially riskier because of that. Nonetheless, investors appeared to have adored SASB deals over the past decade. However, CMBS issuance, including that of SASB deals, has slowed considerably this year. Year-to-date in 2013, only $10 billion of SASB deals and $12 billion of conduit deals have hit the market. As interest rises sharply and liquidity tightens up in the credit market, tougher times might be ahead for CMBS market overall, and particularly for the riskier ones.

[1] For example, the maximum LTV ratio for commercial loans to receive an "A" rating by MorningStar is 0.61. "U.S. CMBS Single-Asset/Single-Borrower Ratings Methodology." *MorningStar* (June 2018). < https://ratingagency.morningstar.com/PublicDocDisplay.aspx?i=s9EtxkUMPSc%3d&m=i0Pyc%2bx7qZZ4%2bsXnymazBA%3d%3d&s=LviRtUKXqs8kml5dHt7FTeE2SZmY0Fvqd4iX49Mk%2f9UapyiFTE06TA%3d%3d>.

Figure 1: *Non-Agency CMBS Issuance, 2013 to 2023*

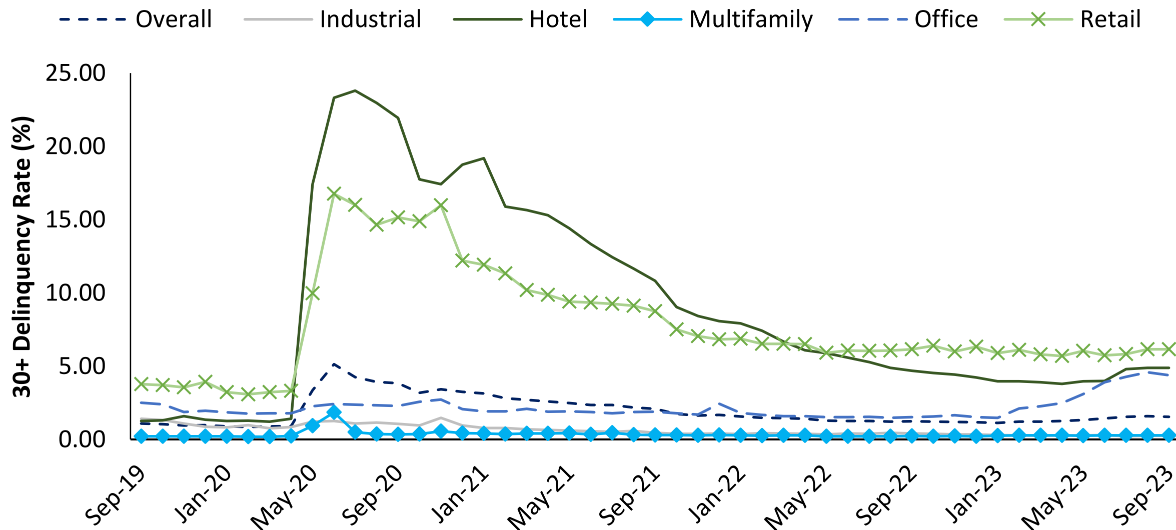


Performance Strong Overall but Hotel, Office, and Retail Loans Under Pressure

At the onset of the Covid-19 pandemic, delinquency rate among CMBS loans (including agency loans) spiked, especially among the hotel and retail segments. *See* **Figure 2**. While the 30-plus-day delinquency rates for hotel and retail loans have fallen drastically since then, they have yet treated to the pre-pandemic levels. For hotel loans, the delinquency rate hovers around 4 percent, compared to less than 2 percent before the pandemic. For retail loans, the delinquency rate stabilizes at roughly 6 percent, compared to just a shade above 3 percent before 2020.

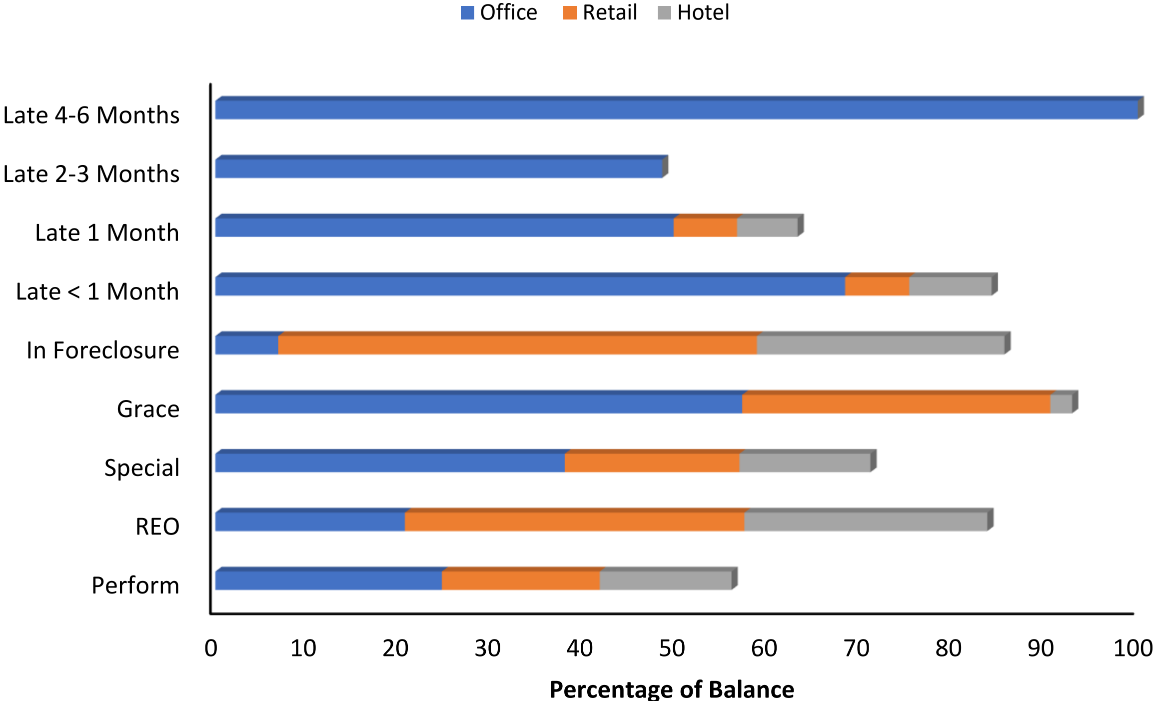
Also there has been a notable uptick in the delinquency rate for office loans this year. Across the nation, office building vacancy rates have been on the rise. See our article on this topic here.

Figure 2: *30-Plus-Day Delinquency Rate for All CMBS Loans (Including Agency Loans)*



Among our sample of non-agency loans, we find similar performance statistics. Roughly 5.5 percent of outstanding balances are non-performing (i.e., Specially Serviced, REO, Foreclosure, or Delinquent). As expected, non-performing loans tend to have greater exposure to the sectors for which sustained or accelerating delinquency rates have been observed, i.e., hotel, office, and retail spaces. **Figure 3** shows the difference in exposure to these sectors by performance status. Among performing loans, roughly 56 percent of loan balance is tied to hotel, office, or retail properties, much lower than the average of 79 percent for non-performing loans. In fact, loans that are two-plus-months delinquent are entirely collateralized with office buildings.

Figure 3: *Exposure to Office, Retail, and Hotel Spaces by Loan Status*



Realized Losses at $2 Billion

Cumulative realized losses from non-performing loans are a shade over $2 billion, representing just 0.36 percent of the overall balance. There are nevertheless individual deals with massive losses. Two deals have recorded cumulative realized losses of over $100 million.

Table 1 lists the top 10 deals with the highest realized losses so far, with losses ranging from $32 million to $122 million and loss severity as high as 84 percent. Loans in these deals are typically backed by retail, office, or hotel properties, many of which have been liquidated at massive losses during the pandemic.

Take GSMS 2014-GC18, for example. Of the $122 million realized less, $52 million in loss was from a loan for a shopping mall in Pennsylvania, which was liquidated in July 2021. Another $62 million was from a loan backed by a regional shopping mall in Portage, Michigan, which was liquidated in December 2021.

Table 1: *Top Ten Deals with Largest Realized Losses*

Deal	Cutoff Balance (USD Millions)	Realized Losses (USD Millions)	Loss Severity
GSMS 2014-GC18	$205.33	$122.43	60%
TRU 2016-TOYS	$512.00	$104.86	20%
WFRBS 2014-C24	$101.50	$73.38	72%
GSMS 2014-GC20	$80.00	$67.12	84%
COMM 2014-CR20	$103.95	$57.07	55%
COMM 2014-UBS5	$69.88	$46.38	66%
MSBAM 2013-C11	$85.00	$45.49	54%
COMM 2014-CR14	$86.46	$37.86	44%
JPMCC 2015-JP1	$71.20	$34.04	48%
COMM 2013-CR12	$73.01	$32.09	44%

$243 Billion CMBS Loans Maturing Over the Next Three Years

The next three years will see a wave of CMBS loans maturing—$243 billion, to be exact. That represents approximately 42 percent of the total non-agency CMBS loans issued over the last decade. Some statistics flash warning signs of bigger losses ahead. Of the $166 billion loans maturing in the next 18 months, 14 percent of them have LTV above 75%. The data also points to 2025 in particular as a potential year of turmoil. Of loans maturing in the first half of 2025, more than 5 percent of the loans have debt servicing coverage ratio ("DSCR") between 1 and 1.1, a range suggesting vulnerability of the properties to generate enough cash flow to cover debt payments. Of those maturing in the second half of 2025, 10 percent of them have already been placed in special servicing, which is abnormally high compared to other vintages.

For additional inquiries, please contact info@vegaeconomics.com.