Commercial RealEstate Direct

THE YEAR-END

2016

ON THE JOURNEY TO A NEW BEGINNING

STATE OF CRE MARKETS

WHERE ARE WE NOW?
WHAT'S NEXT?

THE GOOD, BAD AND UGLY

BEAUTY IS IN THE EYE
OF THE BEHOLDER

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INSIDE THE YEAR-END

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LETTER FROM THE EDITOR

Orest Mandzy
Managing Editor

The question we hear, and quite frankly, most often ask ourselves is: what is the state of the CRE market? If this were a journey, as our cover suggests, some might say we're at a new beginning. Personally, I prefer a baseball allusion: most signs indicate that we're in extra innings, with some saying that we're actually in the second game of a double-header. In the end, the perspective depends on how optimistic you are.

We try to let the data guide us. So far, things are going relatively well.

What we consider the belly of the wall of maturities has been addressed with surprising efficiency. While the commercial real estate sector isn't out of the woods yet, worries that delinquencies would skyrocket so far have proven overblown. The CMBS sector, however, still faces more than $117 billion of maturing loans this year. You could almost see the light at the end of the tunnel.

Property values have continued to climb, driven by apartments and central business district offices; there's still plenty of liquidity in the mortgage business; construction activity has been kept in relative check, mortgage delinquency levels are low and loan-underwriting practices remain disciplined. But the market is facing headwinds, and you can sense an impending inflection point.

Interest rates are on the increase, which could hobble the run-up in values. Meanwhile, risk-retention rules are now fully in place. And banks are facing growing capital set-aside rules and restrictions on their commercial real estate lending activity.

In this issue of the *Year-End*, our third such edition, we explore some of the issues the industry faces and what could happen. Some might get a sense of *déjà vu*.

This issue also includes the latest version of our annual *Commercial Real Estate Derby*, a cheat-sheet that's a reader favorite for gauging the probability of refinancing for some of the largest maturing CMBS loans.

We've also included our *Year-End* CMBS Awards—our league tables—in which we rank bookrunners, loan contributors, servicers and B-piece buyers. Topping the bookrunner race is JPMorgan Securities. Last year was the first year in five that Deutsche Bank didn't take top honors.

I hope you enjoy this edition of the *Year-End* and find the information we've compiled useful. As always, we look forward to your feedback. Have a happy and prosperous New Year.

Best Regards,

Orest Mandzy

The State of the Commercial Real Estate and CMBS Markets: Implications for Commercial Banks

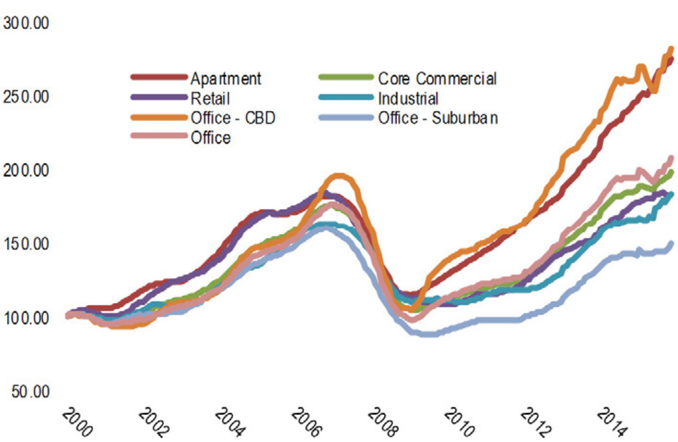
By Tom Fink

How Did We Do in 2016?

The CMBS market appeared to recover in 2015 and 2016, but new-issue bond spreads, which determine prices, have continued to fluctuate. They were especially hard hit during the first half of last year. The same was true of CMBS in the secondary market. The silver lining in the 2016 commercial real estate market: treasury rates remained low and property values continued to improve.

But they haven't improved uniformly. Since the financial crisis, overall commercial real estate values have recovered handsomely, and are now 22.3 percent greater than they were during their pre-recession peaks. However, that was driven by the apartment sector and by properties in major markets. Apartment values, for instance, are up 50.8 percent since prior to the recession—absolutely blowing away all other property types, according to Real Capital Analytics. Meanwhile, properties in major markets are up 38.7 percent. Those in non-major markets are up only 8.4 percent from their pre-recession levels.

CRE Value Indices - 2016

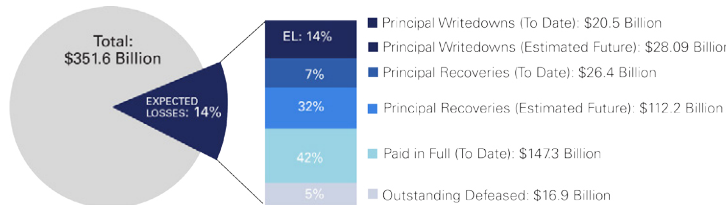


Source: Moody's/RCA Commercial Property Price Index

Low Treasury rates, relatively tight bond spreads and rebounding property values have driven the market liquidity that has allowed many of the sins from the heady days of 2006 and 2007 to be forgiven. We can see that in the overall decline in the CMBS delinquency rate, despite recent upticks. At the same time, projections of how many loans from 2006 and 2007 would suffer losses have declined sharply. Some research had anticipated that more than 50 percent of those loans would get hit. At this point, our research shows that fewer than 20 percent of the 2006/2007 vintage will experience a loss.

So far, loans from the 2006/2007 era have suffered about $20 billion of losses. Based on Trepp LLC analysis of the current performance of the remaining CMBS collateral from those years, there may be another $28 billion of losses from those vintages.

Expected Losses From Loans: 2006-2008



Source: Trepp LLC

Meanwhile, $147 billion of the $351 billion of loans securitized during those years has paid off and another $17 billion have been defeased, or replaced by government securities. Trepp expects another $112 billion from those years to be repaid in full.

The Concerns

The volatility that plagued the market during the first half of last year prompted CMBS lenders to pull back. At the same time, other major lender types—life insurance companies, the housing finance agencies and banks and thrifts—were operating at or near capacity. Luckily, foreign capital stepped in, particularly for trophy properties in major markets. That capital, however, could be fickle. It's dependent on the prices of commodities, such as oil. And if commodity prices decline, the volume of capital it spawns and gets sent to the U.S. also would decline.

While the overall commercial property market remains strong, various sectors are getting pinched. Houston, for instance, is being challenged by issues facing the energy market. In addition, the multifamily market might be reaching the point where overbuilding in some areas could be a concern. And many older shopping malls, particularly those in secondary markets and dependent on department stores like Macy's, Sears and JCPenney, continue to struggle.

As previously noted, volatility in the market makes it difficult to accurately price loans, impacting the volume of CMBS loans that get originated. When that happens, large regional and community banks generally step in to fill the void, which could create a situation similar to the savings and loan crisis that was brought on by excess commercial real estate lending at the height of the market.

CMBS Matters

CMBS didn't exist in the 1980s. When it was developed during the late 1990s, it took a significant market share, primarily from life insurance companies, banks and S&Ls.

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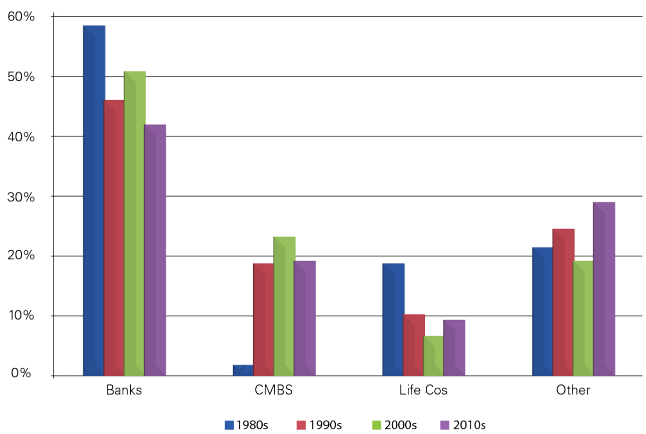
Banks have continued to maintain a significant market share, generally providing about 40 percent of all commercial real estate loan capital. During the 1980s, they provided about 60 percent. They're moving back toward that level.

Their growth has come at the expense of CMBS lenders, life companies and even the housing-finance agencies, which provide capital only to multifamily properties. Each of those investor types has seen an erosion in market share over the years.

Will CMBS be able to rebuild its market share to pre-recession levels?

Lender Market Share
Shifts in Roles Since 1980s



Source: Trepp LLC

Risk Retention and Its Possible Impacts

Much hinges on the impact of the risk-retention rule, a policy that was part of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which was signed into law in 2010. The rule requires the issuer of any asset-backed security to retain 5 percent of the credit risk of any deal it issues. CMBS issuers are allowed to retain a 5 percent vertical strip, by par value, a 5 percent strip of junior bonds, by market value, that can be passed on to a qualified B-piece buyer, or a combination of the two.

A small number of CMBS deals that were designed to be compliant with the risk-retention rules priced last year. All were well received by investors, commanding very tight spreads.

But the downside is that the new requirement will impact the volume of issuance, with many expecting volume this year to range between $65 billion and $70 billion—in line with last year's issuance, but down nearly 30 percent from that reached in 2015. The driver: fewer lenders able or willing to participate and higher costs for borrowers.

Trophy properties, long a mainstay of the CMBS market, could become increasingly difficult for securitized lenders to finance in that single-borrower deals typically haven't included a B-piece. They too will have to abide by the risk-retention rules.

What Does This Mean for Banks?

If CMBS lending isn't as active as it historically has been, fee income for the dominant CMBS originators—all banks—will necessarily decline. Equally important, the largest servicers in the CMBS market are also banks. They too will see a drop in fees.

The Winners Will Be ...

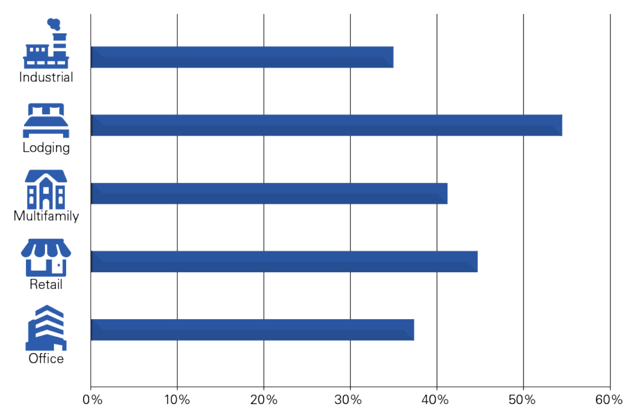
Life insurance companies would appear to be among the winners in the new world because more quality assets will be available for them to lend against. And banks that participate in the syndicated loan market for commercial real estate also will see their market shares increase as some single-borrower deals might migrate to the loan syndication market.

The Losers ...

Well, CMBS issuers will continue to see their market share erode. Borrowers also lose out because debt capital likely will become more expensive. More importantly, secondary and tertiary markets could see a drying up of capital, which could have an impact on regional and community banks.

Banks historically have provided debt for properties under construction or in some type of transition. Such loans are meant to be short- or intermediate-term in nature. CMBS has been a major source of refinancing capital for those loans. Research shows that about 30 percent of CMBS loans provided take-out financing for those types of bank loans. In the case of hotel loans, almost 50 percent of all CMBS loans provided take-out financing.

Loans Transferring to CMBS Within
Three Years of Construction/Renovation



Source: Trepp LLC

Secondary and tertiary markets definitely stand to lose if CMBS shrinks dramatically. Morgan Stanley researchers found that CMBS provided as much as 50 percent of the debt capital for retail properties in tertiary markets and 40 percent of the capital for properties in secondary markets.

By dollar volume, CMBS' biggest exposure is to the 10

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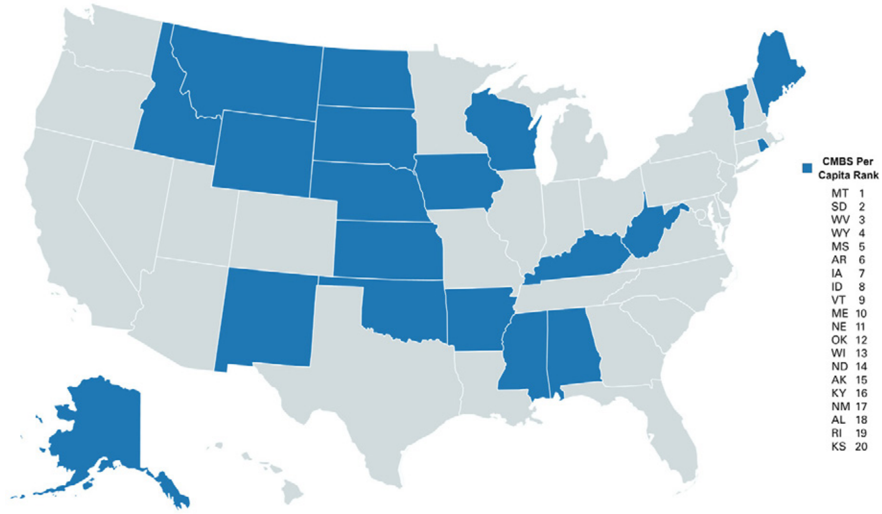
Largest States Using CMBS Per Capita



Source: Trepp LLC

largest states in the country. But that stands to reason. Under any broad measure of economic activity, you'd end up with the same 10 states. Looked at on a per-capita basis, CMBS has been a critical source of real estate debt capital in states such as Montana, South Dakota, West Virginia, Wyoming and Mississippi.

If banks were to pick up the slack from CMBS, many would exceed the commercial real estate concentration guidelines set forth by their regulators. Creating that much pressure on banks could potentially create a situation where factors that led to the S&L crisis are repeated.

So, as competition fades as CMBS shrinks, banks will get the upper hand, with more control over pricing. They'll get to pick up market share in a loan category they're familiar with and with less competition. Theoretically, they can be pickier and get the better credits, particularly in those secondary and tertiary markets. Hopefully, that would translate to a safer book of business for them.

On the other hand, many banks would be the sole source of capital for commercial real estate in their respective markets. They also would have fewer take-out financing options for their construction and transitional loans. So all banks could face longer-duration mortgage assets, increasing their interest-rate risk.

A Repeat of the S&L Crisis?

With CMBS playing a shrinking role in the market for commercial mortgages, banks would be adding market share while real estate values are reaching their peaks—reminiscent of the S&L crisis of the late 1980s.

If we're reaching the end of the current commercial real estate cycle, wouldn't making CMBS a smaller player push banks into increasing their commercial real estate exposure at the worst possible time? ■

Tom Fink is a Senior Vice President and Managing Director at Trepp LLC.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2016 Was Another Disappointing Year for CMBS Issuance

By Orest Mandzy

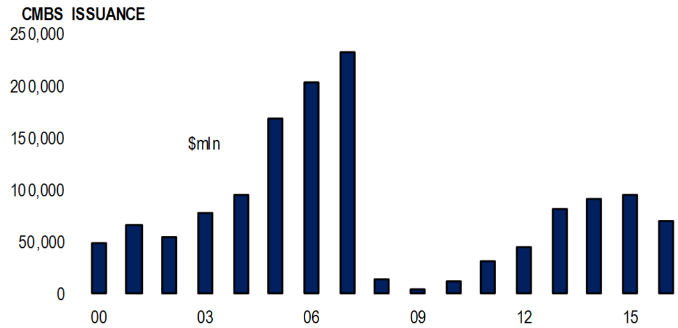
CMBS issuance fell by nearly 30 percent last year to $68.3 billion, marking the first annual decline in issuance since 2009.

That shouldn't have happened. A total of $87.1 billion of loans, mostly originated in 2006, were scheduled to mature during the year; interest rates remained at historically low levels and property sales activity remained robust. Those all would normally be solid predictors of increased issuance. Indeed, projections in late 2015 had called for issuance last year to climb to between $100 billion and $125 billion.

But the bond market didn't cooperate. CMBS got trapped in a global widening of bond yields that started in mid-2015, as investors demanded greater compensation for the risks they took on. Commercial mortgage originations, at least from securitized lenders, ground to a near halt early in the year as it became challenging to profitably price loans amid the volatility. Lenders that had grown accustomed to 2 percent profit margins from the loans they sold into securitization all of a sudden faced losses.

Spreads for benchmark bonds—those with the highest ratings, 30-percent subordination and 10-year lives—had widened sharply during the latter half of 2015 and bounced wildly between 120 and 140 basis points more than swaps. They bounced around and hit a high of 173 bps more than swaps for a deal that priced last March. A year earlier, deals were pricing at levels that were half that. Uncertain where spreads would be on any given day, issuance was sharply cut. April and May each saw only two conduits get done. June saw none.

CMBS Issuance 2016



Source: Commercial Real Estate Direct

As a result of the market volatility, the second quarter saw only $9.5 billion of issuance. Lenders that continued to write loans jacked up their loan spreads or wouldn't quote rates until closing, which they often delayed as much as possible.

Conditions gradually stabilized as would have been expected given the dearth of second-quarter issuance. But lenders and issuers remained cautious. As, too, were investors, as they preferred deals from established issuers affiliated with commercial banks and penalized those from others, effectively tiering issuers.

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The cautiousness became evident in deals' underwritten credit metrics. Conduit loan-to-value ratios averaged 64.3 percent in 2015. For all of last year, it had improved to 59.9 percent. The 33 conduit deals that priced during the second half boasted a 58.7 percent LTV ratio.

Debt-service coverage ratios also improved. Deals that priced in the second half of the year had a 2.14x DSCR, up from 1.82x for all of 2015. Debt yields, meanwhile, have climbed substantially. The deals that priced during the second half of last year had an average yield of 11.28 percent, marking a reversal, as debt yields consistently had been shrinking.

That improvement in collateral quality is highly unusual. During the last market cycle, lenders became increasingly generous in terms of leverage and coverage.

Meanwhile, issuance volumes picked up near the end of the year. November, for instance, saw $11 billion of issues, easily topping issuance for the entire second quarter. December saw $5.3 billion of deals.

The expectation is that issuance will be flat or maybe decline yet again this year, as issuers grapple with risk-retention rules that went into effect on Dec. 24. While four compliant deals were issued last year, and each was well received by investors, the industry is still in knots. Many in the market don't expect much more than, say, $70 billion will be issued. Some outliers have issuance reaching $80 billion, but much depends on just how willing issuers are to retain 5 percent of each deal they issue, or the types of premiums B-piece buyers will need to invest in the horizontal strips.

So stay tuned. The market's in for an interesting ride. ■

2H - 2016 Conduit Issuance

Px Date	Trepp Abbr	Amt $mln	Top 10 %	AAA-JrLvl	BBB-Lvl	UW DSCR	IO%	Part IO%	PX10 AAA	PXJR AAA	PXBBB-
1-Jul	SGCMS 2016-C5	736.81	43.40	23.13	8.38	1.78	31.90	22.90	138	170	760
8-Jul	JPMCC 2016-JP2	939.20	53.10	21.75	7.38	1.81	28.00	44.90	122	145	
15-Jul	WFCM 2016-C35	1022.88	40.40	23.25	8.13	2.02	18.50	35.00	115	140	600
14-Jul	CGCMT 2016-P4	721.16	50.90	23.25	8.25	1.69	23.10	49.40	118	135	
26-Jul	DBJPM 2016-C3	893.74	64.00	21.63	7.38	2.04	47.60	22.60	108	123	
4-Aug	WFCM 2016-BNK1*	870.56	58.70	21.88	7.00	2.35	37.50	28.90	94	110	425
11-Aug	CD 2016-CD1	703.22	66.60	19.50	6.50	2.48	33.90	34.90	100	120	
11-Aug	CGCMT 2016-C2	609.17	59.30	25.00	8.38	2.13	32.30	41.20	106	120	515
12-Aug	MSC 2016-UB11	719.76	65.60	21.63	7.00	2.27	23.80	16.10	105	125	485
14-Sep	WFCM 2016-LC24	1045.36	38.00	21.00	7.38	2.00	22.50	34.50	108	150	625
22-Sep	JPMCC 2016-JP3	1217.49	49.80	20.25	7.00	2.12	44.70	25.50	108	135	520
22-Sep	GSMS 2016-GS3	1068.34	62.10	21.25	7.00	2.49	40.70	30.40	106	135	520
26-Sep	MSBAM 2016-C30	885.23	56.50	21.00	7.25	2.53	36.70	33.60	111	142	560
29-Sep	WFCM 2016-NXS6	757.13	57.70	23.63	8.38	2.02	50.00	13.60	117	162	630
30-Sep	CGCMT 2016-P5	917.43	48.40	21.50	7.50	2.11	35.10	24.10	115	160	615
7-Oct	COMM 2016-COR1	890.68	54.20	24.00	8.00	1.88	51.80	24.30	120	160	
21-Oct	WFCM 2016-C36	858.18	50.80	21.00	6.88	2.30	30.60	12.50	115	150	600
25-Oct	MSBAM 2016-C31	953.19	49.70	23.13	8.25	1.94	10.80	46.90	118	160	615
31-Oct	JPMDB 2016-C4	1124.38	51.90	21.75	7.25	2.16	31.60	41.10	111	135	525
1-Nov	CFCRE 2016-C6	787.54	56.60	22.50	7.38	2.40	48.00	15.30	117	145	610
3-Nov	CGCMT 2016-C3	756.49	56.30	21.63	7.00	2.23	41.10	16.40	114	135	565
4-Nov	MSC 2016-BNK2*	725.57	60.00	22.38	7.63	2.22	36.70	22.80	107	130	480
10-Nov	CSAIL 2016-C7	767.63	52.80	23.13	8.50	1.72	8.60	39.80	120	165	700
16-Nov	GSMS 2016-GS4	1026.54	65.80	21.00	6.75	3.04	47.00	25.50	102	122	490
18-Nov	CD 2016-CD2*	973.39	66.90	26.00	7.88	2.21	61.80	25.90	100	114	
22-Nov	WFCM 2016-LC25	954.97	37.90	22.50	6.85	2.16	11.30	52.80	116	150	700
22-Nov	MSC 2016-UB12	824.44	62.40	23.88		2.13	35.90	16.40	112	130	605
6-Dec	CGCMT 2016-P6	913.41	44.90	25.00	8.50	1.94	42.30	28.40	114	145	570
5-Dec	JPMCC 2016-JP4	997.64	56.30	24.00	7.25	2.22	37.00	28.30	110	132	575
6-Dec	MSBAM 2016-C32	906.95	50.10	22.75	7.75	2.14	31.10	36.40	113	140	565
9-Dec	WFCM 2016-C37	750.51	54.30	22.25	7.50	2.04	25.60	30.00	112	140	565
9-Dec	CFCRE 2016-C7	652.91	61.90	23.50	7.75	2.15	50.50	15.60	118	150	565
14-Dec	CSMC 2016-NXSR*	606.83	66.20	25.000	8.000	1.94	47.70%	10.80%	115	140	

Source: Commercial Real Estate Direct
** Denotes Risk-Retention Compliant*

Washington Outlook: Capital and Liquidity Remain Key Focus in 2017

With a new presidential administration and Congressional session this year comes hope for change in public policies affecting commercial real estate.

By Martin Schuh and Christina Zausner

At this writing in early December, there is more speculation than concrete facts about the incoming Trump Administration and the 115th Congressional agenda. We know, however, that this will be a year full of potential for public policy changes affecting commercial real estate finance.

Reading the tea leaves, the Commercial Real Estate Finance Council believes that the regulators will continue apace and that certain members of Congress will continue their efforts pushing for revisions to the Dodd-Frank Act, as well as general changes to overall Federal rule-making procedures, such as requiring cost-benefit analysis. We also expect policymakers to put forward tax reforms with features that will affect commercial real estate lending and investment.

Assuming that debate about financial and tax reforms extends into 2018 and that there will be positives and negatives for the CRE sector, the greatest game-changing policy shift in 2017 may be monetary. Even though the market is expected to absorb increased rates without dislocating, any change in benchmark rates still has the potential to add stress into market dynamics, especially as refinancings mount.

Here are key pieces of the puzzle CREFC sees in play in 2017:

Regulatory

• **SEC/CFTC Market Oversight Agenda Will Likely Align More with the Trump Administration's Agenda**. With five of 10 commissioner seats vacant at the Securities and Exchange Commission and the Commodity Futures Trading Commission, the complexion of market oversight is bound to shift and mirror that of the Administration's more closely in 2017 and beyond. For sure, we expect a greater level of resistance to new rulemaking in the realm of market oversight.

• **... But the Banking Agencies' Course Depends on Early Retirements/Vacancies**. The banking agency agenda may remain on its current path until 2018, unless sitting officials decide to retire early. Assuming that Fed Chair Janet Yellen and Vice Chair Stanley Fischer remain in place through their terms, agenda change would need to be driven by other Fed governors, particularly Dan Tarullo (the Fed's lead governor on regulation) and the leadership at the Federal Deposit Insurance Corp. and the Office of the Comptroller of the Currency. If current leadership maintains its majority through 2017, critical issues for the industry, including capital, liquidity, risk retention and the Volcker rule, are unlikely to be changed without Congressional intervention.

• **International Rulemaking Bodies Tending to Final Banking Requirements; Still Determining Key Positions on Market Oversight and Nonbank Supervision**. International rule-setting bodies are in the end-game of most bank-related requirements, but also are continuing to build their non-bank and market frameworks.

• The Basel Committee on Banking Supervision (BCBS) has targeted year-end 2016/early 2017 for adoption of critical banking requirements, including final changes to risk-based capital (also known as Basel IV), which represent the last major thrust of bank regulation that will apply broadly to the industry. The International Organization of Securities Commissions has been developing a set of policies and principles that address securitization. At this time, we believe they will coordinate with the BCBS on the "Simple, Transparent and Comparable" framework (which corresponds to Europe's STS, or Simple, Transparent and Standardized program) and they will independently continue to perform peer reviews and assessments of G20 countries' market oversight.

• **Significant Capital and Liquidity Rules Set to be Adopted in 2017**. Assuming that the principals at the banking agencies remain in place, we believe that the Basel rules slated to be finalized in 2017, including the Net Stable Funding Ratio and extensive changes to the risk-based capital regime, will proceed on target. This means finalization of U.S. rules this year and conformance targets set for next year.

Legislative

• **Financial Legislative and Tax Reform May Not Gain Momentum until 2018**. CREFC expects that both Houses of Congress will conduct hearings, if not actually propose, some form of relief from financial services regulation in 2017. It will likely be contemplated as a stand-alone piece of legislation and not as part of this year's budget plan. Expect hearings to begin sometime in the first quarter.

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The most relevant bill to the commercial real estate industry appears to be from many months back, when the chairman of the House Financial Services Committee, Jeb Hensarling (R-Texas), introduced a bill to undo some of the more controversial parts of the Dodd-Frank Act. Called the "Financial CHOICE Act," it contains myriad provisions, but those directly affecting CRE are the repeal of risk retention; repeal of the "Franken Amendment" for credit rating agencies; repeal of the "Volcker Rule;" a requirement that Congress approves of any major new rules; and finally an "off ramp" for well-capitalized banks to avoid many of the regulatory burdens that resulted from Dodd-Frank, including Basel compliance.

On the tax front—given much attention during Election 2016—Trump and House Speaker Paul Ryan (R-Wis.) are in about 80 percent agreement. Of course, details will need to be fleshed out during the next Congress, but the underlying principles in the House Blueprint are:

• Reduce the top C-Corp tax rate to 20 percent from 35 percent and cap the S-Corp tax rate at 25 percent. Individual tax rates are the same in both Trump's and Ryan's plans at 12 percent, 25 percent and 33 percent. Trump proposed further reducing the C-Corp rate to 15 percent.
• Allow for the full and immediate depreciation for capital expenditures.
• Shift the U.S. to a territorial tax system.
• Carry forward net operating losses indefinitely.

Rules Harmony Between U.S. and European Commission. Because our friends over at the European Commission, or EC, favor less burdensome treatment for derivatives, wholesale funding and securitization under capital and liquidity regulations, we believe that Congress may have additional incentives to try to influence capital and liquidity rulemaking in the U.S.

The EC is actively adopting certain exclusions and mitigations that apply to securitizations. The EC's November 2016 version of the Net Stable Funding Ratio is another important example of divergence between the regions. If the European Union continues to move toward lower level thresholds, then it is in Congress' interest to try to align our regulation with theirs so as not to disadvantage the U.S. in the global arena. Look for hearings in the House to exploit this disparity in the coming months. ■

Christina Zausner is vice president, industry and policy analysis, and Martin Schuh is vice president, legislative and regulatory policy, of the CRE Finance Council.

The Wall of Maturities: Looking Back and Forward

By Karina Estrella

Last year, the CMBS market moved into the belly of the so-called "wall of maturities," with $126.8 billion of loans having come due.

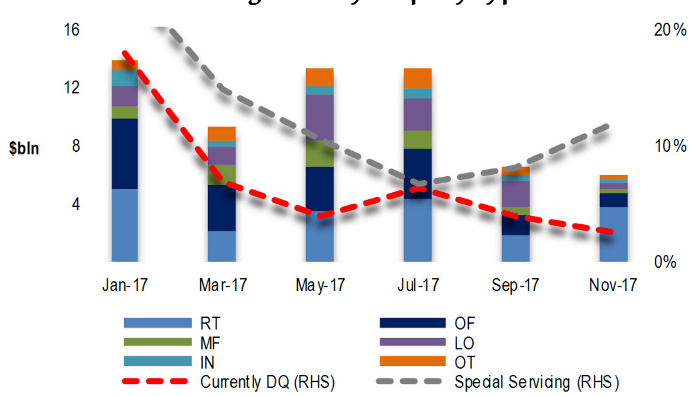
But thanks to historically low interest rates and healthy real estate fundamentals, 69.1 percent of that volume paid off at or before their maturity dates.

Another 2.7 percent of the total was paid off after maturity and $7.53 billion of loans, or another 5.8 percent of the total, suffered losses at pay off. That leaves about 21.7 percent of what had come due during the year still outstanding.

Of the loans that suffered losses, those against retail properties were hit the hardest, with a 52.2 percent loss severity. Office and hotel loans were right behind, with loss severities of 45.38 percent and 45.41 percent, respectively.

The wall of maturities, which started in 2015, was built by the unprecedented levels of CMBS issuance between 2005 and 2007, when a total of more than $600 billion of bonds were issued. Because most CMBS loans have 10-year terms, the bulk of them are now coming due. The wall subsides in 2018, when only $17.6 billion of loans come due.

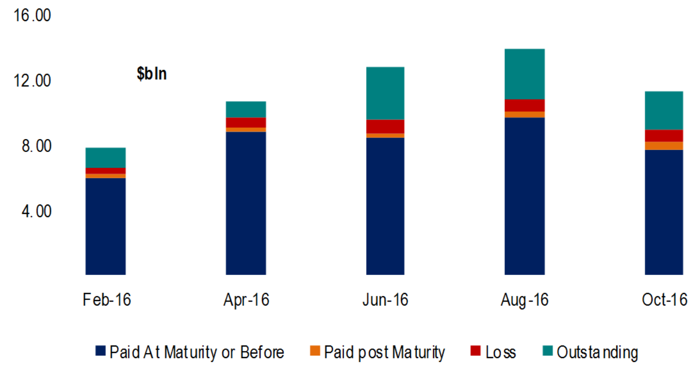
Maturing Loans by Property Type



Source: Trepp LLC

This year, $117.2 billion of CMBS loans come due. Office loans represent 30.7 percent of that total, while retail

2016 Maturities



Source: Trepp LLC

loans comprise about 27.9 percent. They have the highest delinquency rates for the vintage, 6.6 percent and 6.9 percent, respectively.

The retail sector continues to raise the most concern for potential refinancing troubles, given its high delinquency rates and heavy loss severities. The distress often has been tied to the large number of retailer bankruptcies and the decision by national players to reduce their store counts.

An example of retail-loan distress: the $114.4 million mortgage against Marley Station, a 1 million-square-foot shopping center in Glen Burnie, Md. The loan, which was securitized through Banc of America Commercial Mortgage Corp., 2005-3, originally had come due in 2012. But because of property performance issues—inline occupancy had fallen below 60 percent—it was unable to get refinanced. The loan transferred to special servicing that same year and ultimately went through foreclosure.

The long-suffering collateral property was sold last month at a Ten-X auction for $21.5 million, which likely will result

Maturity Year

	2016	2017
As of	4Q 2015	4Q 2016
Wall LTV	76.55	81.67
Wall DSCR	1.78	1.50
Wall Cap Rate	6.58%	7.67%
Wall Debt Yield	12.65%	13.38%
DQ Rate	7.93%	5.86%
National DQ Rate	5.17%	5.03%

Source: Trepp LLC

in the loan suffering more than $100 million of losses.

An example of a suffering office loan is the $203.3 million Lafayette Property Trust mortgage that's securitized through JPMorgan Chase Commercial Mortgage Securities Corp., 2007-LDP10. The loan comes due in March and clearly will have challenges getting taken out. Its collateral, nine properties with 839,469 sf in the Washington, D.C., suburb of Alexandria, Va., was appraised in November at a value of only $110 million. The loan is in the hands of special

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Retail Property Sector Stabilizes Despite Onslaught of Challenges

By Jen Loukedis

The retail property sector continues to evolve, with technology driving much of the change. Many owners of retail properties are embracing that change as an opportunity, but what does the future hold?

To understand where retail is going, let's take a look at where it was.

In 2011, the United States was emerging from the Great Recession. The retail-property sector was struggling with weak demand, despite little construction. According to Reis Inc., vacancy rates for malls and shopping centers hovered at about 9 percent and 11 percent, respectively, and were increasing. Also, construction was at a decade-long low. Only 83,000 square feet of neighborhood and community shopping center space was added during the first quarter of that year, the lowest quarterly volume since at least 1999.

The increasing vacancy rates were driven by retailer bankruptcies and weak consumer spending. E-commerce also started eating into brick-and-mortar businesses. According to the U.S. Department of Commerce, e-commerce accounted for 4.5 percent of the $1 trillion of total adjusted retail sales volume in the second quarter of 2011. So it's no surprise that retail rents were flat or down during that time in 45 of the 80 markets that Reis tracks. Words like "bleak," "weak" and "delinquent" dominated the retail-property conversation.

The sector continues to struggle with anchor-tenant closures. But landlords have started to adapt by seeking non-traditional tenants—yoga studios, urgent-care medical centers, grocery stores and entertainment venues—to fill any voids. So mall vacancies have remained in the 7.8 to 7.9 percent range since the third quarter of 2013. Vacancies at neighborhood shopping centers have been stuck at about 10 percent since early 2015.

New space is being added, but volumes have been tempered. Only 1.6 million sf of neighborhood and community shopping center space was brought online during the first quarter, down from 2.3 million sf in the fourth quarter of 2015.

So things appear to be stabilizing, and rents are actually increasing. Asking rents for non-anchor tenants in regional malls turned the corner in the third quarter of 2011 and have steadily increased to $42.20/sf from $38.81/sf. It took until the first quarter of 2013 for effective rents at community shopping centers to move consistently positive. They have increased to $17.79/sf from $16.64/sf.

Some argue that the U.S. might be "over-stored," that is, there's simply too much retail space. CoStar Group estimates that the country has 48.3 sf of retail space per person. While that's down from the nearly 50 sf/person seven years ago, it dwarfs every other country.

Traditional retailers will use technology to enchance their in-store shopping experiences. That may suggest that retailers might shrink the spaces they occupy, using their stores more as showrooms.

So, whither the retail sector? PwC, for one, expects high-end malls to continue to thrive, while other property types, including power centers and lower-end regional malls, will suffer. The hope is that entertainment venues will fill the voids created by the departure of what were traditional retailers at malls.

Meanwhile, we should expect to see more instances of e-commerce merging with brick-and-mortar stores.

Traditional retailers will use technology to enhance their in-store shopping experiences. That suggests that retailers will shrink the spaces they occupy, using their stores more as showrooms. Meanwhile, more e-commerce retailers are expected to open select brick-and-mortar shops. Amazon.com just did that with its Amazon Go grocery store that's being tested in Seattle.

PwC argues that retail landlords, in order to be successful, will have to plow capital into helping their locations enhance the consumer experience. ■

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servicer C-III Asset Management and is in the foreclosure process.

Looking ahead, only 5.86 percent of the $117.2 billion of loans coming due this year are delinquent. And 9.9 percent are in special servicing. In addition, their weighted average debt yield is 13.4 percent, which compares with a 12.7 percent debt yield for loans that matured last year. But their weighted average loan-to-value ratio is 81.7 percent. That compares with a 76.55 percent LTV for loans that came due last year. And their weighted average debt-service coverage ratio is 1.5x, down from 1.78x for last year's maturities.

If interest rates continue inching up, the volume of loans that face refinancing challenges are sure to grow. ■

Wall of Maturities Becomes Low Hurdle; Bridge Lenders Chomp at the Bit

By Orest Mandzy

The wall of maturities has been part of the commercial real estate vernacular for at least two years. The worry was that a large percentage of the volume of loans originated during the market's peak, when underwriting practices were at their frothiest, wouldn't qualify for refinancing as they matured and would drive a huge increase in delinquency.

So far, the wall hasn't been the issue that was feared.

In fact, more than three-quarters of the $126.8 billion of loans that came due last year were paid off. And while delinquency volumes increased slightly during the year's waning months, they didn't increase to panic-inducing levels.

"We haven't seen much distress," explained Gerard Sansosti, executive managing director of HFF. Many thanks ought to be given to historically low interest rates and the abundant liquidity in the commercial real estate sector.

"I don't expect there will be a void," Sansosti said, in addressing the maturities. Indeed, the Mortgage Bankers Association expects mortgage origination volume this year to climb to $537 billion, from the $515 billion of volume it had expected for all of 2016.

But it won't all be smooth sailing. Banks and thrifts, which historically have held roughly 40 percent of the country's commercial real estate loans, are facing regulatory pressure to ease their exposure to the sector. And CMBS, which was hobbled during the first half of last year as market volatility took its toll, will be dealing with newly implemented risk-retention rules. Those rules are expected to limit origination volumes, keeping the sector's contribution to the overall mortgage universe to less than $80 billion. Many expect volumes to range between $55 billion and $75 billion.

The two other big investor groups that fund mortgages are life insurance companies and the housing-finance agencies. Any increases in their volumes will be marginal.

The MBA calculates that $208 billion of mortgages held by all investor types will be coming due this year. A total of $117.2 billion of that is held by CMBS trusts. When most of those securitized loans were written, many didn't amortize, so their balances could be at the inflated levels they were a decade ago. Meanwhile, their collateral very well could be tired and in need of updating. Of course, some of the best loans that were coming due already have been refinanced—many have been defeased, the process of replacing a loan's collateral with government securities. As a result, a large chunk could face challenges getting taken out.

"The remaining (loans) isn't the highest quality," noted Patrick C. Sargent, an attorney with Alston & Bird, who was president of the Commercial Real Estate Finance Council between 2009 and 2010. He noted that much of what's left likely will need help, either in the form of additional equity or other capital that could be used to fund the redevelopment or improvement of their collateral.

Those loans are what Tad Philipp, director of commercial real estate research at Moody's Investors Service, called "zombie loans." They're performing well enough to remain current with their payments, but not well enough to get refinanced.

That's where the growing number of bridge lenders come in.

"The great thing about commercial real estate finance is the diversification of capital sources," explained Thomas Kim, head of the MBA's commercial/multifamily group. Any regulatory tamping of capital flow is picked up by others. Seeing the potential opportunity among the securitized loans coming due, A10 Capital in 2015 started funding permanent loans. The Boise, Idaho, non-bank lender, which also focuses on bridge loans, is backed by a number of significant capital partners and keeps its originations on its balance sheet.

"There will be an opportunity for alternative, stable capital," explained John Spengler, A10's chief strategy officer. "There will be a real desire" among borrowers not to tap securitized lenders because of the restrictions CMBS loans bear. "We also think it's difficult to do business with banks."

In part that's because of the regulations they face, as well as their ambiguity. One need look no further than the rules that govern capital set-asides for loans considered high volatility commercial real estate, or HVCRE, loans that could have a profound impact on the availability of construction financing.

So it's no surprise that there's been substantial growth in the alternative lending space. That growth, however, could result in a squeeze on existing bridge lenders.

"Lenders aren't capital constrained," noted John Wilcox, managing director and head of lending at Ten-X, an online auction platform. But they will, however, be cautious when lending against certain property types or areas.

That abundance of capital has changed the dynamics in the bridge-lending business. "Two and three years ago, it was much easier and lower-risk to be a bridge lender," said Larry Grantham, managing director of Calmwater Capital of Los Angeles. "The margin for error has decreased and not everyone will be a winner."

Most bridge lenders were created to help facilitate acquisitions—they would provide short-term debt capital to fund a property's purchase and subsequent improvements, to enhance its value and allow for a take-out by a larger permanent loan. However, many are finding their businesses shifting to refinancings.

Last year, for instance, JCR Capital saw roughly a quarter of its bridge-lending business involve refinancings. That's going to grow this year, according to Jay Rollins, co-founder of the Denver investment manager. Borrowers "who thought they'd get permanent loans will turn to bridge loans," he predicted.

The timing would be uncanny. The bridge loans would start coming due just when the CMBS market would be facing a dearth of maturities and could be scouring for opportunities.

Only $17.6 billion of CMBS loans come due in 2018. Subsequent years will see subdued maturities as a result of the low issuance volumes 10 years prior. So the bridge loans that are written this year should find plenty of permanent mortgage liquidity. ■


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Office Sector Ends Year with Haves and Have-Nots

By Josh Mrozinski

Investors last year continued to pour money into core office properties in gateway markets, but remained less enthusiastic about properties in secondary and tertiary markets.

Whether those trends continue remains to be seen, as some investors have started re-focusing their attention to non-core areas in their search for yield. Meanwhile, demand for middle-market properties, those valued at roughly $50 million or less, remains spotty, as prospective buyers might be concerned that the market's at or near its peak, while sellers are clinging to unrealistic expectations.

"You're going to see a lot more volatility in 2017," warned Jay Rollins, managing principal of JCR Capital, a Denver investment manager that specializes in the middle market.

Outside of apartment properties, central business district office properties were the big beneficiaries of strong investor capital flows into real estate since the recession. Institutional investors, both domestic and foreign, plowed capital into the best properties in the country's top cities, viewing them as money-good.

Indeed, through October, Manhattan saw the sale of 130 office properties with 21 million square feet for $19.6 billion, accounting for 17.7 percent of the $110.8 billion of office properties that changed hands throughout the country last year.

Driven in part by that activity, prices for CBD office properties, as of last October, were 43.7 percent higher than they were during their previous peaks in 2007, according to the Moody's/RCA Commercial Property Price Indices. But prices for suburban office properties, meanwhile, remain 6.6 percent lower than their previous peaks, as investors eschewed what they viewed as riskier properties in uncertain areas.

Capitalization rates, which have an inverse relationship to prices, declined during that time by 30 basis points to 5.3 percent for CBD offices, according to Real Capital Analytics. Suburban office cap rates have barely budged over the past year and remain at 6.9 percent.

With prices for CBD offices climbing so rapidly, investors have started to look afield, kicking the tires in select non-major or secondary markets that they viewed as having relatively healthy and diverse economies. Their thinking: yields would be better if they selectively picked the best properties in those markets.

Indianapolis was a beneficiary. Last year through October, 29 properties sold for a total of $662.1 million, with prices resulting in average cap rates of 6.3 percent. That compares with the 50 properties that sold for $469 million for an average cap rate of 8.7 percent during the same period a year earlier, according to Real Capital.

The same thing happened in Las Vegas, where investors last year through October bought 30 properties for $365 million, for a 5.5 percent cap rate. That compares with 32 property sales for $279.7 million, for a 7.3 percent cap rate, a year earlier.

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Growth in Supply Impacts Hotel Sector

By Jenny Robinson

Last year, developers were expected to bring 841 hotels with 95,346 rooms online, and this year they're expected to add another 1,056 properties with 118,638 rooms, according to Lodging Econometrics.

That would represent a 3.1 percent increase in the country's inventory of rooms over the past two years and could contribute to a softening of fundamentals.

Most markets have hit their peaks in occupancy, according to Steve Hennis, vice president of consulting and analytics at STR. He's projecting a small decline in occupancy and rate growth this year. That would be the first annual decline since 2010.

Room additions had peaked in 2008, when 1,341 properties with 154,257 rooms were added. That was just as the recession hit. Growth in revenue per available room, or RevPAR, a closely watched performance metric that combines occupancy and room rate, had declined by 2 percent that year. The following year, it fell by a whopping 16.6 percent, according to PwC.

With hotel performance so weak, development activity naturally ground to a halt as lenders disappeared into the woods. In 2010, for instance, the country's inventory of rooms increased by a mere 0.2 percent. That compares with the annual average of 2.4 percent for the three previous years.

When travel started picking up and hotel occupancy rates started increasing in 2010, developers started building again. They've been bringing the sector back to its historic norm. Additions remained at less than 1 percent until 2015, when inventory grew by 1.4 percent, according to PwC, which relied on data from STR, a Hendersonville, Tenn., hospitality research firm.

"From a supply-growth perspective, we're in check, just below industry norms," explained J.P. Ford, senior vice president and director of business development at Lodging Econometrics. He added that lending practices haven't gotten out of hand. "There is disciplined lending, so development isn't out of whack nationwide."

While demand for rooms has remained healthy, some markets are getting pinched because of the construction. For instance, STR reports that New York City had 15,276 rooms under construction as of the end of November, a 14.8 percent increase from last year. The city has a supply of nearly 115,000 rooms. So those in the construction pipeline would represent a 13.3 percent growth in the number of rooms in the city.

That's had an impact on RevPAR. Last April, for instance, STR had New York City's RevPAR down by 2.3 percent.

Houston's another troublesome market. It had 5,608 rooms under construction in November. While much less than what it had under construction a year earlier, it still is a robust number given the area's 83,814-room total inventory. RevPAR earlier in the year was down by 7 percent, STR noted.

Both markets have been flagged by Moody's Investors Service as being the most vulnerable to short-term declines in occupancy and rates, largely because of the number of rooms coming online.

Other markets, such as San Francisco, Washington, D.C., and Tampa, Fla., are expected to outperform, with CBRE Hotels projecting an average daily-rate increase of more than 6 percent this year.

Performance data indicate that the business cycle for the hotel sector is getting long in the tooth. RevPAR had been increasing by at least 5 percent annually since 2010. In 2011, it climbed by a whopping 8.1 percent, thanks to a 4.2 percent increase in the country's occupancy rate, to 60 percent, and a 3.8 percent increase in average daily rates. The following year, RevPAR grew by another 6.6 percent. In 2014, it again rose by 8.1 percent, due to a 3.4 percent spike in occupancy to 64.4 percent—an indicator that demand far outstripped growth in supply. That allowed hotel owners to increase their rates by 4.5 percent.

While room rates have continued to increase at a healthy pace, occupancy increases have softened. PwC and others expect a drop in occupancy next year.

CBRE Hotels, meanwhile, projects that the sector's occupancy rate will slip to 65.3 percent this year from last year's 65.4 percent—an all-time high. It expects room rates to increase by 3.3 percent.

The current and expected softening has translated to a drop in the prices investors are willing to pay for properties, according to Lodging Econometrics. Last year through September, 671 hotels changed hands at an average price of $136,934/room. That was down 13 percent from a year earlier. Hotels with more than 200 rooms each saw an even larger price decline, 26 percent, while resort property prices declined by 37 percent. ■

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Cap rates in Indianapolis and Las Vegas compare favorably to some major markets, particularly Chicago, at 6.5 percent, and Los Angeles, at 5.6 percent.

"There is no shortage of capital," said Lance Patterson, founder of Patterson Real Estate Advisory Group, an Atlanta boutique capital markets advisory firm.

Patterson said prices have room to run in certain secondary markets, particularly in those where the cost to build remains higher than the cost to buy. He pointed to Atlanta and Nashville, Tenn.

The cost to build anew in Atlanta is $425/sf, he said, whereas the top price for an existing property last year was $366/sf. That property was Ten 10th St. Union Investment Real Estate, a German fund manager, purchased the 410,624-sf property, which is 91 percent occupied.

Meanwhile, the pick-up last year of construction in certain markets has raised flags. Manhattan, for instance, will see 1.9 million sf of additional space come online, according to Reis Inc. But absorption will outpace that, which will further improve the market's occupancy rate to 91.4 percent.

Rent growth, however, is starting to slow. Last year, rents climbed by 3.3 percent, according to Reis. While impressive, it pales in comparison with the 6-percent growth registered a year earlier.

That's prompted many investors to lower their pricing expectations, according to James Murphy, executive managing director of Colliers International. ■

CMBS Investors Not Compromising Quality as Investors Chase Yields

By Jim Costello

Commercial property prices as measured by the Moody's/RCA Commercial Property Price Indices have posted year over year gains since 2010.

As pricing gets ever higher, the pressure to stretch for yield grows. This stretch for yield is evident in a downshift in the average quality of what has been selling in the office market, even as average capitalization rates trend lower and lower. CMBS lenders, however, have exhibited a curious reaction to this shift in quality, with more financing on the high end of the office market and less in the middle.

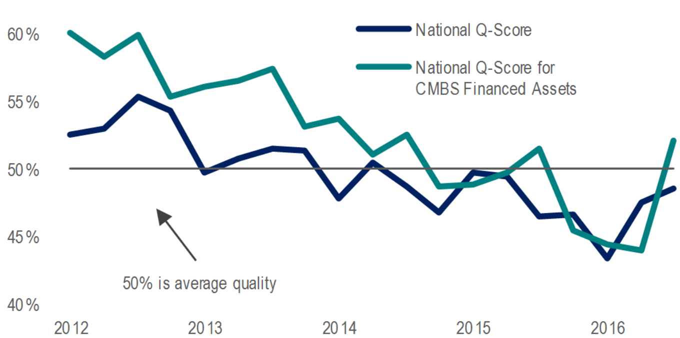
Following the global financial crisis, there was a flight to quality. Investors were risk averse and focused on high-quality properties in the large gateway markets. Into the recovery, with those assets priced at a premium and investors willing to take on more risk, the quality of acquisitions started to fall and has consistently declined since 2012.

Stretching for yield can mean a number of things, but generally investors are faced with the decision of buying lower-quality properties in major markets or high-quality properties in secondary and tertiary markets. One challenge here is that "quality" can be a subjective topic.

The Average Quality of What Is Selling in the Office Market Fell as Cap Rates Fell

Using Q-Score, a measure of quality recently developed by Real Capital Analytics, we can now objectively measure the quality of assets that have traded and the CMBS market's reaction to it. Q-Scores effectively rank each asset from 1 to 100 percent, based on the value of each property relative to all others in that market at the time. These scores incorporate not only physical attributes, but also market and locational factors as well.

National Q Score, 3-Period Average

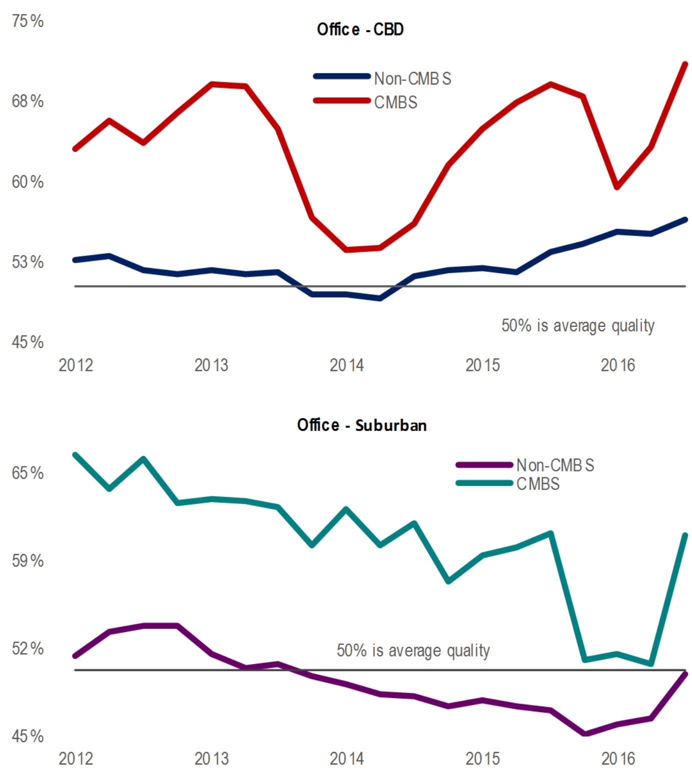


Source: Real Capital Analytics

National Q-Scores provide a ranking of each asset relative to all others in the country, while Local Q-Scores are based solely on properties within that market. For example, the best office tower in Oklahoma City is not going to achieve pricing comparable to a tower on Fifth Avenue in Midtown Manhattan, so its National Q-Score may be rather modest. However, its Local Q-score would be very high. In a period of normal market liquidity one might expect an even mix of high- and low-quality asset transactions that would generate average Q-Scores that are close to 50 percent.

In part, the downward trajectory of the National Q-Scores for what has sold since 2012 is a function of deal activity

Local Q Score



Source: Real Capital Analytics

moving out from the major markets to the secondary and tertiary markets, where investors are not willing to pay the same high prices for assets.

Property transaction trends of CMBS lenders versus non-CMBS lenders show a clear flight to quality by securitized lenders in the office sector over the last year.

Flight to Quality in Office Market by CMBS Lenders into 2016

In the aftermath of the so-called "Taper-Tantrum" of 2014, office properties sold in suburban markets and central business districts, or CBDs, expanded to include lower-quality assets. A year earlier, those same lower-quality

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properties found it difficult lining up financing. Both CMBS and non-CMBS lenders exhibited changing patterns of what they would lend on, though the relative pace of movement on the part of securitized lenders was far greater. These lenders had been making loans only on the top one-third of CBD office assets in each local market into 2013. But a year later, as the financial markets stabilized, these lenders moved to a mix of assets in the top 45 percent of each market.

Into 2016, the CMBS market faced challenges with B-piece buyers stepping back early in the year in the face of bond-market turmoil. Our Q-Score indicators show that CMBS lenders responded by sweetening their offerings with higher-quality assets.

Within the CBD office market, these lenders had been lending on the top 40 percent of assets into the end of 2015. But by the third quarter of the following year, they had tightened their standards and lent on assets that on average were among the top 30 percent of all buildings within their respective markets. These lenders also moved to tighten up the quality of assets they lent against in suburban submarkets.

In response to the pullback by B-piece buyers due to market turmoil, CMBS lenders, more so than other lenders, moved to issue loans against higher-quality assets. With these higher quality assets tied to their securities, they hoped to entice B-piece buyers to take on risks they previously wouldn't.

Investors sometimes can go too far in their stretch for yield, as a property cycle matures. Even as cap rates plumb new depths, however, CMBS lenders did not stretch to issue loans against lower-quality assets last year. ■

Jim Costello, CRE, is senior vice president of Real Capital Analytics, a New York data and analytics company.

Investor Interest in Apartments Sees No Signs of Slowing

By Josh Mrozinski

The bull run in the national apartment sector shows no signs of slowing.

Last year through October, a total of 6,121 apartment properties sold for $121.4 billion, according to Real Capital Analytics. That compares with the 6,549 properties that sold for $119 million during the same period a year earlier.

Prices for apartments, meanwhile, recorded a 12 month gain of 12.6 percent in October, according to the Moody's/RCA Commercial Property Price Indices. And capitalization rates, or the yields that investors are getting from their investments, in 2016 had dropped to 5.7 percent from 6 percent a year earlier, according to Real Capital Analytics.

Investors continue to be drawn to the sector largely because of demographic trends. And that's not expected to change anytime soon. While an increase in interest rates might result in an increase in cap rates, and a corresponding drop in pricing, that remains to be seen. The spread between cap rates and Treasury yields is lower by between 53 and 84 basis points than historical averages, according to Stewart Information Services Corp., which relied on Real Capital data.

So it would stand to reason that prices would decline if Treasury rates continue their upward trajectory. But other factors are used to determine cap rates, including tax rates and alternative investment options. For now, investors remain smitten with apartments, which they view as stable investments.

The sector began its rebound shortly after the market trough in 2008. Apartments initially had benefited, both from an investment and fundamental perspective, from what then was a broken residential lending market. People unable to qualify for a mortgage to fund the purchase of a home, rented apartments or houses by necessity. That still stands true as it remains more difficult for many to qualify for a home mortgage than before the crisis.

On top of that, growing numbers of people have decided to move to urban or other densely populated areas, to be closer to their places of work and to entertainment venues. So developers started to push the accelerator on new projects.

"I just don't see a lot of weakness," said Blake Okland, vice chairman and head of U.S. multifamily at ARA Newmark, adding, however, that there might be some adjustment in prices as the cost of financing increases.

As demand for units increased, rents were pushed higher, which drove developers to build further. Construction hit its trough in 2011, when only 42,666 units were added. The development pace grew annually after that and jumped by 66 percent in 2013, when 136,823 units were added, according to Reis Inc.

Demand remained healthy, with nearly 300,000 units getting absorbed, or newly leased between 2012 and 2013. Absorption has remained healthy, but during the last three years has been overtaken by the number of units that have been added.

Between 2014 and 2016, 603,739 units were added to the 10.7 million-unit universe, while 536,193 units were absorbed, according to Reis.

Nonetheless, occupancy has remained healthy. It's expected to slip because of the new construction, but it'll remain above 95 percent through at least 2020. Last year, Reis projected the year to end at a 95.4 percent occupancy rate.

Some landlords, meanwhile, are offering concessions, often in the form of periods of free rent in order to draw tenants.

Reis projects that effective rents, which take concessions into account, will increase by 3.2 percent this year. While impressive, it compares with the 3.7 percent increase posted last year. The moderation is happening after a five-year run during which rents appreciated from 22 percent for class-A properties to 24.9 percent for class-B properties.

"Nationally, you can still make the case we were under-built, but are starting to reach historic equilibrium," said Okland.

He noted that banks have started to pull back the reins on construction lending, which will help limit new supply.

Increasing rates are causing some uncertainty, resulting in a number of owners pulling back on their plans to sell their properties. But the higher rates could bolster demand as they would make it even more challenging for tenants to become homeowners. ■

The Good, the Bad, and the Ugly: 2016

By Manus Clancy

It's been said that "beauty is in the eye of the beholder." The quote is credited - for those who are curious - to 19th century Irish novelist Margaret Wolfe Hungerford. When looking at the CMBS market, however, we've been unanimous in our idea of what is good, bad and ugly.

A nice, juicy office lease renewal at higher rates? That's good. An announcement that a large retailer, say Macy's or Sears, would be closing more stores? That's bad. And a lower appraisal for a trophy office, hotel or retail property? That's usually ugly.

But 2016 often provided plenty of heated debate when trying to discern good from bad, or beautiful from ugly. From Brexit to the U.S. presidential elections, and Cleveland (and the Cavaliers) to Chicago (and the Cubs), there usually was a large demographic that saw downright ugly in the outcome.

Bad and Ugly Headlines from 2016

- **January**: General Dynamics announces plan to leave Falls Church, Va., office backing big 2014 loan.
- **February**: $94.3 million Gateway Salt Lake loan modified - note represents over 30 percent of the collateral behind the JPMCC 2010-C1 deal. Modification would later be reversed.
- **April**: Four loans known as the Empirian Portfolio have been sent back to special servicing. Together, the notes make up almost 25 percent of the remaining collateral behind MLMT 2007-C1.
- **June**: Value of UBS Center in Stamford, Conn., cut by more than 80 percent from its securitization appraisal. The loan makes up almost 75 percent of the remaining collateral behind LBUBS 2004-C1.
- **September**: Golfsmith files for bankruptcy.
- **November:** Failure of some maturing 2006 and 2007 loans to refinance push CMBS delinquency rate back over 5 percent.

Even things that normally trigger stink eye - increasing interest rates - were met more favorably than usual. After years of microscopic Treasury yields, personal investors, insurance companies and pension funds were certainly thirsting for better returns.

As we write this piece, the 10-year Treasury rate was hovering at about 2.5 percent. Commercial real estate players have to be asking themselves when will the tipping point occur that leads to the beginning of value erosion?

That's not the only question facing the CMBS sector this year. With risk retention kicking in last month, guesses are far and wide as to exactly what the cost will be in terms of loan spreads and yearly issuance. And with a new administration coming to Washington, opinions range from "count on it" to "not a chance," when it comes to rolling back regulations.

On other topics, the CMBS market so far has handled the 2016 wave of mortgage maturities much better than it handled the swell of maturing five-year loans in 2012. Back then, the delinquency rate hit its highest level ever, largely because many of those five-year loans didn't pay off at their maturity. Last year, thanks to continued low rates and healthy commercial real estate value growth, the maturities largely muddled through. In addition, it was still worthwhile for borrowers to lock in low-coupon loans, even if they had to defease their existing loans, an often costly process.

The Bad and Ugly

In the spirit of consistency, we will begin with last year's lowlights - the bad and the ugly - with the caveat that even ugly stories often had silver linings. Take, for instance, the $363 million loan against Atlanta's Bank of America Plaza. It was resolved with a loss to two 2006 CMBS deals after the collateral property, with 1.25 million square feet, was purchased by Shorenstein Properties. The loss—55.7 percent—was much smaller than was predicted a few years earlier.

New-issue volume reached just more than $68 billion last year, excluding collateralized debt obligations and agency transactions. The volume was well below last year's predictions and lower than the $95.1 billion of volume recorded in 2015. Much of the decline was the result of a bad start to 2016.

An early, angry equity sell off helped create a great deal of volatility in the fixed-income markets last year. CMBS spreads blew out, leading securitized lenders to either stop quoting loans or quote loans at non-competitive levels. The result was a second quarter that was the weakest quarter for issuance in more than four years.

The Good

Even though the year began on a sour note, the second half of 2016 proved to be robust. New issue volume was strong; the market remained unfazed by "anti-establishment" votes in the United Kingdom, the United States and Italy; and optimism grew that perhaps the costs of complying with risk retention would not be as great as once feared. Several risk retention eligible deals were "tried out" by issuers and were extremely well received by investors. ■

Good Headlines from 2016

- **January**: $3 billion Stuyvesant Town/Peter Cooper Village loan pays off at par after collateral is sold for more than $5 billion.
- **January**: Citigroup will exercise its option to purchase 388 & 390 Greenwich St. in Manhattan's Lower West Side. The 2.6 million-square-foot complex backs the single loan securitized through the CGCMT 2014-388G deal.
- **February**: CMBS delinquency rate hits multi-year low of 4.15 percent.
- **June**: Brexit "Yes" vote has minor impact on CMBS market, which quickly finds its legs. Third-quarter issuance volume rebounds sharply.
- **August**: CMBS new-issue spreads hit tightest levels of year.
- **October**: $410 million Manhattan Collection loan defeased.
- **December**: Pre-risk retention issuance remains high; Optimism grows that cost of risk retention will not be as material as once feared.

The 3rd Commercial Real Estate Derby

Analysis by
MANUS CLANCY

Refinancing Odds for 2017

Purse: $12 Billion
Post Time: January 1, 2017
Track Condition: Muddy
Distance: 1 3⁄16 miles

Program number represents poll position.

Despite disparaging remarks made about the class of 2007, many of the largest loans to mature over the next 12 months look likely to refinance. A muddy track – risk retention kicking in and higher long-term interest rates - makes nothing a sure thing, but the prospects are generally good for the largest loans.

Disclaimer: Odds are purely fictional and do no represent true odds of each loan paying off.

FIVE TIMES SQUARE — 2-1

1

Loan Balance: $1,076,000,000
Maturing Date: March 2017
Sires: WBCMT 2007-C30, WBCMT 2007-C31
The Skinny: Ernst & Young is the 1.1 million-square-foot property's largest tenant, but it's been said to be considering alternatives; pays a base rent of $50/sf. The midtown Manhattan property, the first of three in the race, also has subordinate debt. It's fully occupied, but debt-service coverage ratio (on net cash flow) was only 1.11x for 2015.

SHORENSTEIN PORTLAND PORTFOLIO — 1-1

2

Loan Balance: $697,200,000
Maturing Date: April 2017
Sires: GSMS 2007-GG10
The Skinny: Consists of 16 office properties totaling about 4 million sf in the Portland, Ore., area. DSCR (NCF) from 2011 to 2014 was under 1.0x, but numbers (and occupancy) have come up in recent years. The borrower, Shorenstein Properties, is confident in its ability to refinance the debt. Loan-to-value ratio at securitization was 66 percent, and no subordinate debt helps.

WELLS FARGO TOWER — 3-1

3

Loan Balance: $550,000,000
Maturing Date: April 2017
Sires: GSMS 2007-GG10
The Skinny: Top three tenants at the 1.4 million-sf property make up more than 50 percent of its rent roll and all have extended since loan was originated. No large short-term leases coming due. Market has been improving, but DSCR still less than 1.0x.

DDR SOUTHEAST PORTFOLIO — 1-1

4

Loan Balance: $883,000,000 (Rounded)
Maturing Date: July 2017
Sires: CGCMT 2007-C6, COMM 2007-C9, WBCMT 2007-C32
The Skinny: A total of 52 retail properties with a combined 7.3 million sf supports the loan. Most of the properties are in the southeastern United States. Financials have been steady with DSCR (NCF) consistently 1.25x or better since 2011. Underwritten with LTV of 63 percent.

237 PARK AVENUE — 9-2

5

Loan Balance: $419,600,000
Maturing Date: June 2017
Sires: LBCMT 2007-C3
The Skinny: Occupancy at the midtown Manhattan office property has declined to 63 percent from 89 percent in 2010. DSCR (NCF) under 1.0x for last two years. Property once was home to now-defunct Bear Stearns. Loan was in special servicing several years ago. Considerable subordinate debt against it.

1745 BROADWAY — 1-5

6

Loan Balance: $340,000,000
Maturing Date: Jan. 2017
Sires: LBUBS 2007-C1
The Skinny: The last of the midtown Manhattan office entrants, this one is home to Penguin Random House. The publisher is the sole tenant in the nearly 650,000-sf property. Recent lease extension for it helped seal the deal. Borrower has requested payoff statement and loan should be repaid on time.

WILLIS TOWER (AKA SEARS TOWER) — 1-5

7

Loan Balance: $680,000,000
Maturing Date: Feb. 2016
Sires: LBUBS 2007-C2, JPMCC 2013-WT, LBUBS 2007-C7, LBUBS 2008-C1
The Skinny: The Chicago office tower backs a mix of legacy debt and CMBS 2.0 debt. DSCR and occupancy have been on the rebound, and borrower expects to pay off loan during the open period. Substantial subordinate debt has sat (and may still sit) in collateralized debt obligations.

ONE LIBERTY PLAZA — 2-1

8

Loan Balance: $560,000,000
Maturing Date: Aug. 2017
Sires: GCCFC 2007-GG11, CGCMT 2008-C7
The Skinny: A 53-story office building with more than 2.1 million sf in lower Manhattan. DSCR (NCF) below the 1.0x threshold. Property once was leased to Goldman Sachs, but space was vacated years ago. It was valued at $1.5 billion in 2006. Recently, Zurich North America announced that it would vacate it for space at 4 World Trade.

2016 CMBS Award Winners

JPMorgan Unseats Deutsche at Top of Bookrunner Ranking

By Orest Mandzy

For the first time in five years, Deutsche Bank wasn't the most active bookrunner of domestic, private-label CMBS. It was JPMorgan Securities.

The bank consistently has been among the most active underwriters of deals, and this year it was able to top Deutsche in part due to its large-loan business. JPMorgan was involved in 12 single-borrower transactions totaling $6.7 billion and was sole bookrunner on five of those, which totaled $2.5 billion. It also was involved in eight conduit deals, and was sole bookrunner on two, totaling $2.2 billion. Overall, it got credit for 14.9 deals totaling $10.3 billion, giving it a 15.1 percent share of the year's $68.3 billion of issuance.

Its single-borrower deals included JPMorgan Chase Commercial Mortgage Securities Corp., 2016-NINE, a $900 million deal that was part of a $1.2 billion financing package against midtown Manhattan's 9 West 57th St., a 1.7 million-square-foot trophy office building owned by Sheldon H. Solow. It also was involved in single-borrower deals that financed the Shops at Crystal retail center in Las Vegas, the Palisades Center shopping center in West Nyack, N.Y., and the Hyatt Regency Waikiki Beach Resort & Spa in Hawaii.

Deutsche, meanwhile, also was involved in a dozen single-borrower deals. Those totaled nearly $7 billion. But it was sole bookrunner on only three, totaling $1.6 billion. It shared duties on the others. And it was involved in 10 conduit deals, serving as sole bookrunner on two deals totaling $1.7 billion. Its total tally amounted to 14.2 deals totaling $9.9 billion, for a 14.5 percent share of the market.

Just behind the two was Wells Fargo Securities, which received credit for 13.4 deals totaling $9.5 billion, for a 13.9 percent share of the market.

Commercial Real Estate Direct divvies up credit proportionally among each deals' bookrunners.

JPMorgan's move to the top rung of the ladder was driven by its sector-leading $8.7 billion of loan contributions, which while down just more than 20 percent from a year ago, amounted to one-third more than the amount contributed by Deutsche. Goldman Sachs was second-most active in a ranking of loan contributors, with $7.4 billion of volume.

Issuance last year fell far below expectations and 28.1 percent below the $95.1 billion registered in 2015. That was driven by volatility in the bond market that resulted in a sharp decline in issuance during the first half, when only $26.9 billion of CMBS was issued.

Continued on page 24

Top Managers of Domestic, Private-Label CMBS

	2016			2015		
Investment Bank	**#Deals**	**Bal $mln**	**Mkt Shr%**	**#Deals**	**Bal $mln**	**Mkt Shr%**
Academy Securities	39	30,982.65	45.33	3	1,991.00	2.09
Drexel Hamilton	31	25,009.09	36.59	46	41,446.67	43.58
Citigroup	26	20,525.90	30.03	34	24,503.06	25.77
Deutsche Bank	27	19,714.00	28.85	35	33,646.87	35.38
JPMorgan Securities	22	15,120.17	22.12	23	18,655.51	19.62
Goldman Sachs	19	14,388.13	21.05	21	20,612.26	21.68
Wells Fargo Securities	20	13,654.42	19.98	24	19,723.84	20.74
Morgan Stanley	17	13,057.72	19.11	31	25,470.73	26.78
Barclays Capital	14	9,798.95	14.34	14	12,437.20	13.08
BoA Merrill Lynch	14	9,634.92	14.10	22	17,881.42	18.80
UBS	9	7,080.01	10.36	9	8,577.84	9.02
Cantor Fitzgerald	9	6,820.00	9.98	17	16,923.07	17.80
Natixis	9	6,186.71	9.05	8	8,337.01	8.77
KeyBank	7	5,307.56	7.77	0	0.00	0.00
CastleOak	5	4,010.77	5.87	7	7,592.79	7.98
Jefferies	4	3,660.10	5.36	7	8,056.36	8.47
Credit Suisse	6	3,539.15	5.18	16	12,389.06	13.03
CIBC	3	2,747.83	4.02	9	8,214.46	8.64

Top Bookrunners Domestic, Private-Label CMBS

	2016			2015		
Investment Bank	**#Deals**	**Vol $mln**	**Mkt Shr%**	**#Deals**	**Vol $mln**	**Mkt Shr%**
JPMorgan Securities	14.94	10,350.16	15.14	15.07	12,105.67	12.73
Deutsche Bank	14.21	9,926.60	14.52	18.23	17,210.79	18.25
Wells Fargo Securities	13.36	9,513.96	13.92	17.77	14,715.47	15.61
Citigroup	10.87	8,061.79	11.80	10.79	7,608.49	8.07
Goldman Sachs	10.05	7,563.72	11.07	10.17	8,463.19	8.98
Morgan Stanley	7.36	5,091.85	7.45	14.47	9,715.97	10.30
BofA Merrill Lynch	7.24	4,257.04	6.23	9.70	6,966.40	7.39
Credit Suisse	5.29	3,224.51	4.72	10.75	8,593.95	9.11
Barclays Capital	4.69	3,096.56	4.53	10.18	6,719.75	7.07
Cantor Fitzgerald	4.41	3,019.53	4.42	1.00	140.00	0.15
UBS	3.19	2,432.68	3.56	2.35	2,141.92	2.27
Societe Generale	2.79	1,622.18	2.37	0.13	127.28	0.13
Natixis	0.50	125.80	0.18	0.00	0.00	0.00
KeyCorp	0.10	55.70	0.08	0.00	0.00	0.00
Jefferies	0.00	0.00	0.00	0.32	462.29	0.49
Scotia Capital	0.00	0.00	0.00	0.10	125.00	13.26
Total	**99.00**	**68,342.07**		**121.00**	**95,096.16**	

2016 CMBS Award Winners

Continued from page 22

As bond spreads stabilized, issuance perked up, with the third quarter seeing $18 billion of issuance and the final quarter tallying $23.5 billion. The fourth quarter's numbers were no doubt goosed by issuers pushing to get deals done before risk-retention rules kicked in.

The year's issuance was comprised of 55 conduit deals totaling $47.1 billion, 39 single-borrower deals totaling $19.6 billion, two floating-rate deals totaling $618 million and three others totaling $1 billion.

A ranking that gives full credit to every manager on a deal had Academy Securities at the top, co-managing 39 deals totaling $31 billion, or just more than 45 percent of the year's issuance. The investment bank topped Drexel Hamilton, which held top honors in 2015. Last year, it co-managed 31 deals totaling $25 billion, for a 36.6 percent share of the market.

Both Academy and Drexel Hamilton are disabled veteran-owned institutions. Academy was founded in 2009 by Chance Mims, a former U.S. Naval officer. Its president is Phil McConkey, a graduate of the U.S. Naval Academy who perhaps is better known for his years as a wide receiver for the Super Bowl-winning New York Giants football team.

Drexel Hamilton, meanwhile, was founded in 2007 by Lawrence K. Doll, a former Marine who served in Vietnam, and Marine Corps General Peter Pace. The firm got into the CMBS business four years ago and has been tapped as a co-manager on more than a quarter of the deals issued since. Goldman Sachs is its mentor under the Treasury Department's Mentor-Protégé Program, which is designed to help improve the competitive capabilities of minority-, women- and veteran-owned businesses. Academy's mentor is JPMorgan Securities.

CMBS volumes are expected to remain relatively subdued this year, with most predictions falling within the range of $60 billion to $75 billion, with some outliers. The big headwind faced by the sector is risk retention, which at the least will prompt securitized lenders to write loans with less leverage. That alone would take away one of the big advantages CMBS loans have had over others. ■

Top Loan Contributors

	2016			2015		
Loan Contributor	#loans	Vol $mln	Mkt Shr%	Vol $mln	Mkt Shr%	Difference %
JPMorgan Chase Bank	133.67	8,670.33	13.34	10,858.98	11.55	-20.16
Goldman Sachs	156.20	7,418.37	11.41	6,258.96	6.66	18.52
Deutsche Bank	178.17	6,510.75	10.02	8,867.97	9.43	-26.58
Citigroup	184.41	5,512.20	8.48	6,274.94	6.67	-12.16
Morgan Stanley	113.18	4,130.53	6.36	8,264.67	8.79	-50.02
Wells Fargo Bank	223.85	3,572.32	5.50	6,117.35	6.51	-41.60
Bank of America	141.06	3,240.29	4.99	6,533.69	6.95	-50.41
Cantor Commercial	175.10	3,212.55	4.94	4,325.86	4.60	-25.74
Barclays Bank	118.12	2,959.78	4.55	5,178.16	5.51	-42.84
UBS Real Estate Securities	134.50	2,431.97	3.74	2,699.80	2.87	-9.92
Rialto Mortgage Finance	192.50	1,932.17	2.97	2,412.71	2.57	-19.92
Natixis	109.00	1,895.34	2.92	2,548.32	2.71	-25.62
Starwood Mortgage Capital	133.50	1,739.00	2.68	2,067.73	2.20	-15.90
Credit Suisse	68.65	1,530.18	2.35	5,982.51	6.36	-74.42
Ladder Capital Finance	98.60	1,349.53	2.08	2,584.94	2.75	-47.79
Benefit Street Partners	83.00	1,241.16	1.91	637.28	0.68	94.76
Jefferies LoanCore	57.00	1,110.22	1.71	1,215.69	1.29	-8.68
Societe Generale	51.80	1,083.80	1.67	534.19	0.57	102.89
Silverpeak Real Estate	61.00	771.38	1.19	980.30	1.04	-21.31
KeyBank	73.10	758.05	1.17	855.62	0.91	-11.40
Lonestar/Relius	22.00	506.26	0.78	0.00	0.00	0.00
BNY Mellon	25.00	488.38	0.75	658.98	0.70	-25.89
Principal Commercial	24.00	478.71	0.74	819.12	0.87	-41.56
NCB FSB	100.00	444.78	0.68	274.47	0.29	62.05
C-III Commercial Mortgage	68.00	367.67	0.57	629.35	0.67	-41.58
Bancorp Bank	35.00	367.04	0.57	524.21	0.56	-29.98
CIBC World Markets	28.00	273.73	0.42	1,237.01	1.32	-77.87
MC-Five Mile	26.00	182.71	0.28	1,484.06	1.58	-87.69
Basis Real Estate Capital	18.00	156.01	0.24	397.10	0.42	-60.71
Bank of China	0.20	110.00	0.17	0.00	0.00	0.00
KGS-Alpha Real Estate	18.00	74.73	0.12	102.30	0.11	-26.95
Redwood Commercial	7.00	72.23	0.11	740.49	0.79	-90.25
Liberty Island Group	5.00	67.91	0.10	562.83	0.60	-87.93
Prudential Mortgage	1.00	65.00	0.10	0.00	0.00	0.00
Walker & Dunlop	5.00	55.85	0.09	279.24	0.30	-80.00
RAIT RBS	3.00	21.38	0.03	367.12	0.39	-94.18
Freedom Commercial	3.00	9.53	0.02	93.52	0.10	-89.81
GE	0.00	0.00	0.00	92.43	0.10	
Scotia	0.00	0.00	0.00	125.00	0.13	
Total	**2,874.60**	**64,811.84**		**93,586.90**	**0**	

2016 CMBS Award Winners

Special Servicer Ranking - 2016

	2016									2015		
	Total			Conduit			Single-borrower					
Servicer	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
Rialto Capital Advisors	16	13,477.66	19.70	16	13,477.66	19.70				15	14,672.62	15.40
Midland Loan Services	15	12,139.83	17.80	12	10,994.83	16.10	3	1,145.00	5.80	26	21,055.00	22.10
CWCapital Asset Management	9	7,265.67	10.60	9	7,265.67	10.60				8	7,690.12	8.10
Wells Fargo Bank	12	6,926.30	10.10	1	1,155.93	1.70	10	5,504.80	28.10	21	14,610.55	15.40
Aegon USA Realty Advisors	13	6,349.83	9.30			0.00	13	6,349.83	32.40	6	3,968.35	4.20
LNR Property Co.	7	5,948.51	8.70	7	5,948.51	8.70			0.00	13	12,278.43	12.90
KeyBank	9	5,158.19	7.50	1	973.39	1.40	7	3,847.80	19.60	12	6,974.13	7.30
C-III Asset Management	5	3,919.54	5.70	5	3,919.54	5.70				3	3,320.89	3.50
Torchlight Loan Services	5	3,504.43	5.10	4	3,342.43	4.90	1	162.00	0.80	4	3,959.35	4.20
Trimont Real Estate Advisors	3	1,474.50	2.20			0.00	2	1,193.50	6.10	1	796.59	0.80
Talmage LLC	2	1,155.00	1.70			0.00	2	1,155.00	5.90			
Hudson Advisors	1	506.26	0.70							1	281.50	0.30
Strategic Asset Services	1	264.00	0.40			0.00	1	264.00	1.30	6	3,617.33	3.80
A10	1	251.60	0.40							1	209.80	0.20

Master Servicer Ranking

	2016									2015		
	Total			Conduit			Single-borrower			Total		
	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
KeyBank	21	12,182.23	17.80	4	3,526.43	7.50	16	8,318.80	42.40	21	13,836.90	14.60
Midland Loan Services	16	11,711.05	17.10	13	10,917.72	23.20	3	793.33	4.00	25	20,177.33	21.20
Wells Fargo Bank	61	44,196.44	64.70	38	32,633.81	69.30	20	10,509.80	53.60	68	58,639.53	61.70
A10	1	251.60	0.40							1	209.80	0.20
Berkadia Commercial Mortgage										4	1,965.10	2.10
FirstCity Financial										1	112.70	0.10
Rialto Mortgage Finance										1	154.80	0.20

2016 CMBS Award Winners

Moody's Keeps Dominating CMBS Ratings; Fitch's Market Share Jumps

Moody's Investors Service remained firmly perched atop a ranking of rating agencies in the private-label CMBS market last year.

It was hired to rate every one of the 55 conduit deals and nearly half of the year's remaining issuance, giving it an 83.5 percent share of the overall market. Its share of the market actually increased from 2015, when it rated just about three of every four deals, including every single conduit deal.

But the big story in the ratings agency ranking is the ballooning share of the conduit market that Fitch Ratings was able to garner. It rated all but one conduit transaction and a quarter of the year's remaining issuance, for a total market share of 74.3 percent.

Fitch solidified its position in the CMBS rating agency business in part because of the relative inactivity of Standard & Poor's in the conduit business. The rating agency in early 2015 was barred by the SEC from rating conduit deals for a year. That restriction was lifted early last year. Since then, S&P has rated three conduit deals.

Many investors, predominantly money managers and mutual funds, require that the fixed-income securities they buy have ratings from at least one of what many call the "major" rating agencies—Moody's, Fitch and S&P. With S&P still getting its legs, and issuers hiring Moody's to rate only deals' most senior bond classes, they've turned to Fitch to ensure that their offerings were as palatable to as many investors as possible. That became a bigger deal in 2016 than the previous year as the pool of potential investors often appeared to be thinning, given the volatility that rocked the market during the first half of last year.

Fitch's rise up the ranking has come at the expense of the four other agencies—DBRS, Kroll Bond Rating Agency and Morningstar Credit Ratings—each of which had a drop in market share.

Domestic Private-Label CMBS Rankings - Rating Agencies

	Conduits			Single-Borrower			Total - 2016			Total - 2015		
	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
Moody's	55	47,077.96	100.00	14	8,948.50	45.60	72	57,065.32	83.50	67	68,068.73	73.38
Fitch	54	46,117.98	98.00	7	4,403.00	22.44	62	50,786.55	74.31	55	52,289.02	56.37
Kroll	34	29,957.43	63.60	9	4,334.80	22.09	45	34,894.80	51.06	56	52,021.23	56.08
DBRS	16	13,249.33	28.10	6	3,065.50	15.62	25	17,353.69	25.39	30	26,912.29	29.01
S&P	3	2,315.89	4.90	28	12,236.93	62.36	32	14,889.82	21.79	37	22,364.33	24.11
Morningstar	7	5,936.84	12.60	14	7,244.33	36.92	22	13,687.43	20.03	52	41,253.59	44.47

Trustees Ranking - 2016

	2016									2015		
	Total			Conduit			Single-Borrower			Total		
	#Deals	Bal $mln	Mkt Shr%	#Deals	Bal $mln	Mkt Shr%	#Deals	Bal $mln	Mkt Shr%	#Deals	Bal $mln	Mkt Shr%
Wilmington Trust	56	41,713.15	61.0	34	29,822.52	63.35	19	10,837.80	55.20	58	51,898.93	54.60
Wells Fargo Bank	27	15,834.45	23.20	12	10,091.72	21.44	13	5,154.13	26.30	34	24,453.81	25.70
Deutsche Bank	9	7141.10	10.40	7	5368.10	11.40	2	1,773.00	9.00	12	10,184.31	10.70
USBank	6	3,112.62	4.60	2	1,795.62	3.81	4	1,317.00	6.70	16	8,164.11	8.60
Citibank	1	540.00	0.80			0	1	540	2.80	1	395.00	0.40

2016 CMBS Award Winners

Rialto Stays Atop B-Piece Buyers; Grows Market Share

Rialto Capital Management continued to absolutely dominate the market for CMBS B-pieces last year, buying the subordinate classes of 16 conduit deals totaling $13.5 billion, for a 28.6 percent share of the market.

While its overall volume had declined by roughly $1 billion from a year ago, its market share jumped by nearly 5 percentage points from 23.5 percent. And that was in a market that appeared to be crowded, when compared to previous years. A total of 18 investors bought into conduit deals last year, up from 11 in 2015 and double the number of players in 2014.

The list of new entrants includes Och-Ziff Capital Investments, which bought into two deals, getting credit for 1.74 transactions totaling $1.6 billion. Also new to the list were Basis Investment Group, World Class Capital and Jefferies LoanCore, each of which bought into one deal of roughly $1 billion apiece.

Prime Finance, meanwhile, suddenly has become a force to be reckoned with. It invested in five transactions, receiving credit for 3.1 deals, as it teamed up with partners on each deal, totaling $2.6 billion. That gave it an impressive 5.6 percent share of a market that it hadn't participated in before.

Commercial Real Estate Direct divvies up credit among a deal's investors based on how much of a deal each bought.

Prime, a New York company that also owns a sizable portfolio of apartment units, is better known as a provider of mortgage, mezzanine debt and preferred equity capital. It stepped into the B-piece market early last year after hiring Luke Dann from LNR Property Corp. as head of CMBS investments. It's capitalizing its investments through a fund, Prime Finance B-Piece Fund I LP, and has partnered on transactions with LNR Property Corp. and Ellington Management.

The thinking is that most, if not all, of the investors that participated in the market last year plan to continue doing so, even under the new risk-retention regime. Although every compliant deal that priced last year used a vertical retention structure, deals that were put together with horizontal structures, where a B-piece buyer would buy and keep subordinate bonds equal to 5 percent of a deal's market value, eventually are expected to be floated.

Top Buyers of CMBS Conduit B-Pieces

	2016			2015		
Investor	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
Rialto Capital	16.00	13,477.66	28.63	14.00	14,517.82	23.46
Eightfold Real Estate	9.00	7,911.57	16.81	8.00	8,559.23	13.83
Torchlight Investors	4.00	3,342.43	7.10	4.00	3,959.35	6.40
LNR Property Corp.	3.50	3,172.29	6.74	7.20	7,607.21	12.29
C-III Capital Partners	4.00	3,148.57	6.69	1.00	1,105.17	1.79
BlackRock Realty	3.00	2,910.92	6.18	2.00	1,783.71	2.88
Ellington Management	3.60	2,682.26	5.70	3.50	3,243.61	5.24
Prime Finance	3.10	2,614.26	5.55	0.00	0.00	0.00
Och-Ziff Capital Investments	1.70	1,641.95	3.49	0.00	0.00	0.00
Seer Capital Partners	2.00	1,509.75	3.21	9.30	8,088.57	13.07
KKR Real Estate	1.00	1,026.80	2.18	4.00	4,362.28	7.05
Basis Investment Group	1.00	1,022.88	2.17	0.00	0.00	0.00
World Class Capital	1.00	954.97	2.03	0.00	0.00	0.00
Jefferies LoanCore	1.00	890.68	1.89	0.00	0.00	0.00
Raith Capital Partners	1.00	770.97	1.64	3.00	3,311.50	5.35
Doubleline Capital	0.00	0.00	0.00	5.00	5,343.95	8.64
	55.00	**47,077.96**		**61.00**	**61,882.40**	

Most of the long-time industry players, such as Rialto, Eightfold Real Estate Capital and Torchlight Investors, have raised funds, some specifically for B-piece investments. As a result, they're geared up to buy and hold, as the rules require.

Rialto, for instance, recently raised $1.3 billion for a fund that could grow to $1.75 billion. And Eightfold in November filed with regulators a notice that it had raised $342 million for Eightfold Real Estate Capital Fund V LP. ■

Neglected Commercial Spaces: How Big Is the Problem?

By Holly Tachovsky

Recent tragedy brought to light the dangers of neglected commercial buildings. A deadly fire at a warehouse in Oakland, Calif., killed 36 people. Investors would discover that the warehouse hadn't been visited by a city building inspector in 30 years. The devastating loss of life is a grave reminder of the threat these buildings pose to the people and communities that surround them.

It makes you wonder: How many more buildings like this are there across the country?

BuildFax conducted a study to see how many commercial buildings had not had permitted updates in the last 30 years. And while we can't know exactly how many of them are in a similar state of extreme risk and disrepair as the building in Oakland, looking at building permit activity can provide some astonishing insight.

One of the benefits of the building permit process is that inspectors from the building departments visit the construction site during and after a project to ensure work is done to standard building codes.

We estimate there are more than a half million commercial buildings in the United States that are standing in various stages of neglect due to a lack of maintenance.

Half a Million Neglected Buildings

We looked at the more than 5.2 million commercial properties in our database and took a representative sample, where we have more than 30 years of data coverage. We flagged these properties for permit activity in 10, 20, 30 and 30+ year time frames.

Our findings were startling: 10 percent of commercial buildings haven't had a permitted update in more than 30 years. That means roughly 520,000 properties across the country are in suspect condition. They have the potential to present catastrophic risks to the people and communities that surround them.

Keeping An Eye On Aging Buildings

A total of 14 percent of the properties we sampled had permitted maintenance conducted on them between 21 and 30 years ago. This represents an estimated 780,000 of the nation's 5.6 million property inventory that likely may

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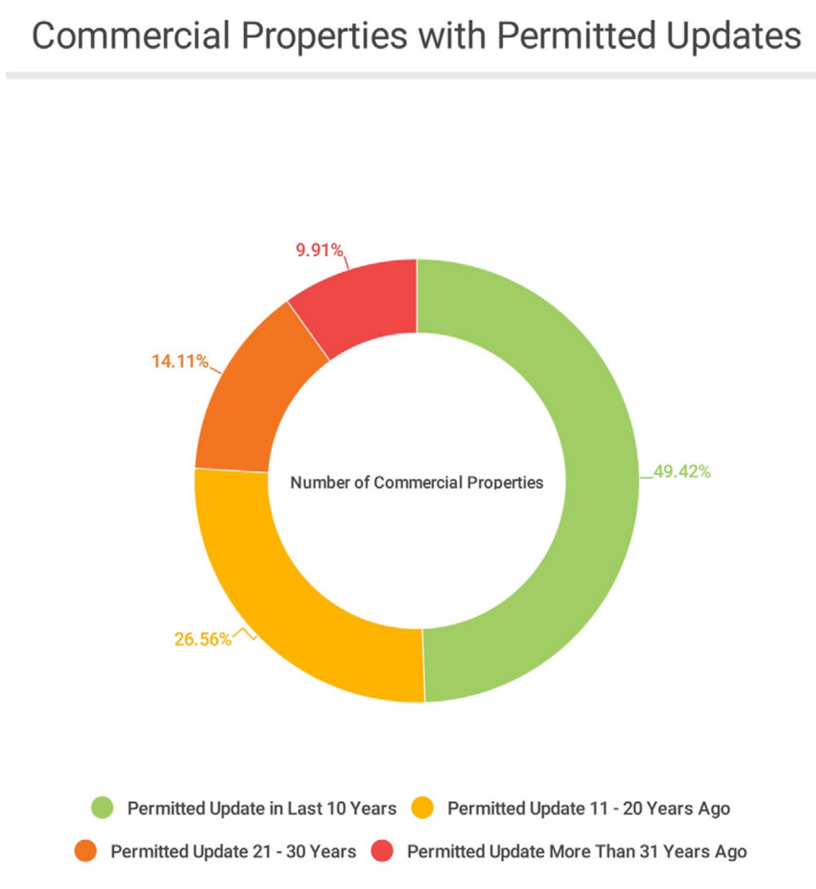

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require updates in the coming years. And if they don't get updated, they risk slipping into the neglected category.

A Majority Maintained

On a brighter note, we found that nearly half of the commercial properties we sampled had a permitted update in the last 10 years. And more than a quarter had a permitted update in the last 20. So roughly 75 percent of the commercial buildings in the country are likely to have been properly maintained and kept up.

Detecting Maintenance and Condition on Older Buildings

One of the benefits of the building permit process is that inspectors from building departments visit the construction site during and after a project to ensure work is done to standard building codes. Trained to identify potentially unsafe conditions, these inspectors are likely to flag other possible code violations. More generally speaking, they're there to make sure buildings are safe for the people who live and work in them.

Much more information about a property can be gathered when a permit is pulled. For example: in order to be granted a permit, the work generally is carried out by a licensed contractor.

What does this mean? Permit activity suggests more favorable property conditions, while long gaps between permit activity correlates to a greater chance a property is in a state of disrepair.

That's evident when it comes to insuring properties. Well-maintained properties are proven to have significantly lower risk for carriers, while poorly maintained buildings, having become compromised over time, result in higher loss rates.

Key Takeaways

Building permits may not prevent tragedies like the one in Oakland, but they call attention to property issues that need to be addressed.

• Maintenance matters—Properties that have had permitted updates are proven to be lower-risk structures.

• There are an estimated half a million commercial properties where maintenance history is unsubstantiated.

• We see strong maintenance history with 75 percent of commercial properties.

Methodology

We analyzed the more than 5.2 million commercial properties in our database and took a representative sample where we have more than 30 years of data coverage. We flagged these properties for permit activity in 10, 20, 30 and 30+ year time frames.

Author's Note

While this data is compelling, we need to keep in mind that the catalyst that inspired this research was a very real tragedy that impacted individuals and families. Our deepest sympathies go out to those affected, both directly and indirectly, by this tragic event. ■

Holly Tachovsky is co-founder and chief executive officer of BuildFax, which maintains a national database of construction permits.

Defeasance Activity Falls Short of Expectations

By Orest Mandzy

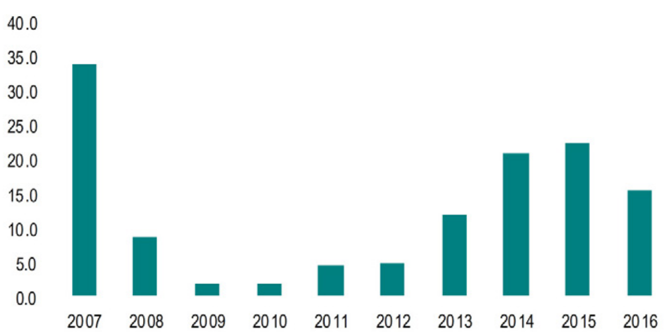
Defeasance activity among CMBS loans declined last year—a surprise given that interest rates remained at or near historic lows for most of the year and overall property values continued on their upward march.

Through the end of November, a total of 1,013 securitized loans with a balance of $15.4 billion were defeased, or replaced by government securities, according to Trepp LLC. That compares with 1,332 loans with a balance of $19.8 billion that were defeased during the same time a year earlier.

The latest year's numbers will grow as additional data is tallied. But total figures for the year will still fall short of the $22.5 billion of loans that were defeased in 2015, according to Moody's Investors Service, which compiles data by surveying the sector's defeasance advisers.

Professionals in the defeasance business had been expecting activity to be comparable to that of 2015. But volatility in the CMBS market crushed those hopes.

Defeasance Volume



Source: Trepp LLC

Property owners, who had become accustomed to CMBS lenders providing loans of 70 percent of a property's value or more, suddenly found themselves in a relatively hostile lending environment as bond market volatility prompted securitized lenders to pull back on the amount of proceeds they were offering.

Out went loans with loan-to-value ratios of 70 percent or more and in came loans with LTVs of 65 percent or less—often much less—particularly for smaller and middle-market properties, the bread and butter of the CMBS business. That's had a heavy impact on defeasance.

Volumes also were impacted by what defeasance professionals say was the "wait-and-see" attitude many borrowers adopted. They were hoping to burn off as much of what could be viewed as the "defeasance penalty" they would face as possible. The closer to a loan's open date that defeasance occurs, the fewer government securities need to be purchased.

Most commercial mortgages come with prepayment restrictions to ensure that lenders receive the cash flows they're expected for the life of their loans. Borrowers choosing to pay off loans before they become open to prepayment would face penalties that often are onerous. They could, however, defease their loans. That is, replace their collateral with government securities that mimic the mortgages' cash flow.

But the process could be costly and time-consuming in that it involves negotiations with servicers and rating agencies, among others, and the selection of appropriate substitute securities. As a result, a number of advisory firms have been formed to specialize in the process. Those include AST Defeasance of Los Angeles; Chatham Financial of Kennett Square, Pa.; Commercial Defeasance and Waterstone Capital Advisors, both of Charlotte, N.C.; Trimont Real Estate Advisors of Atlanta; Bank of America, and Wells Fargo Bank.

Defeasance activity flourishes when interest rates are low and property values high. If a property's value climbs, as generally has been the case, given that the Moody's/RCA Commercial Property Price Index is now 22.3 percent greater than it was at its last peak in November 2007, its owner could refinance the property, through defeasance, in order to access the added equity. That increased value otherwise would remain trapped. But for a defeasance transaction to make financial sense, interest rates typically would have to remain low. Otherwise the benefits of a prepayment could be nullified.

Defeasance Activity

MSA	#Loans	Balance $mln	% of Loans
New York	85	3,160.50	20.57%
Washington, D.C.	24	804.04	5.23%
Boston/Cambridge	12	755.00	4.91%
Chicago	18	488.07	3.18%
Los Angeles	38	477.57	3.11%
San Francisco	13	119.66	0.78%
		5,804.85	**37.79%**

Source: Trepp LLC

Of course, values haven't climbed uniformly across all property sectors. As of last October, prices for properties in major markets were up 38.7 percent from their previous peaks, while those in non-major markets were up only 8.4 percent.

So it's no surprise that loans against properties in the six markets that the CPPI classifies as major accounted for 37.8 percent of all defeasance activity. New York City alone accounted for 20.6 percent of the year's defeasance volume. That was to be expected given the lofty prices certain properties in New York command. Among the biggest loans to be defeased last year was the $625 million mortgage against 9 West 57th St., a 1.7 million-square-foot office

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building in midtown Manhattan. The debt was securitized four years ago through COMM, 2012- 9W57.

The property was appraised at a value of $2.5 billion in 2012, based on its $67.7 million of net cash flow. The $625 million loan that Deutsche Bank then had provided paid an interest-only coupon of 3.787 percent for its five-year term.

That loan was taken out through defeasance last year—it wasn't set to mature until February and became open to prepayment last November—with a $1.2 billion financing package that JPMorgan Chase Bank provided. The securitized debt pegged a $3.4 billion appraised value on the property—a 36-percent increase over the past four years—largely because of recently signed leases that would increase cash flow by nearly 60 percent since 2012 to $107.1 million. It pays an interest-only coupon of 2.86 percent for its full 10-year term.

With interest rates climbing steadily since the presidential election, and the expectation that property values might already have hit their peaks, defeasance volumes may be challenged to keep pace. ■

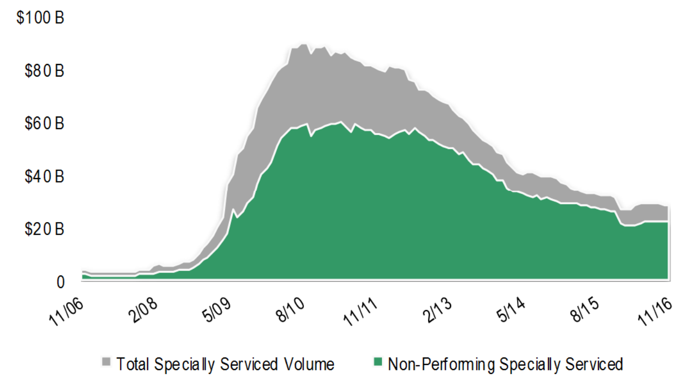
Top Defeased Loans - 2016

Mo. of Defeasance	Bloomberg Name	Vintage	Property Name	Location	Property Type	Balance $mln	DSCR	LTV	NOI $mln	Maturity Date
January	GCCFC 2007-GG9	2007	John Hancock Tower & Garage	Boston	MU	640.50	1.52	50.00	55.34	Jan. 6, 2017
October	COMM 2012-9W57	2012	9 West 57th Street	New York City	OF	625.00	3.76	24.80	90.12	Feb. 6, 2017
November	GSMS 2013-NYC5	2013	Manhattan Collection	New York City	LO	361.70	2.48	47.00	37.80	Jan. 6, 2018
October	GCCFC 2007-GG9	2007	667 Madison Avenue	New York City	OF	250.00	1.49	53.19	21.32	Feb. 6, 2017
August	MSC 2007-HQ11	2007	One Seaport Plaza	New York City	OF	225.00	1.55	46.88	18.26	Jan. 9, 2017
November	COMM 2007-C9	2007	Waterview	Rosslyn, Va.	OF	210.00	1.90	48.26	23.25	June 1, 2017
January	JPMCC 2007-LD11	2007	5 Penn Plaza	New York City	OF	203.00	1.61	67.67	18.58	May 1, 2017
August	COMM 2007-C9	2007	Ritz Carlton Key Biscayne	Key Biscayne, Fla.	LO	160.00	2.96	63.30	29.34	June 1, 2017
December	COMM 2007-C9	2007	85 Tenth Avenue	New York City	OF	150.00	1.27	60.70	19.52	June 1, 2017
June	CD 2007-CD4	2007	The Atlantic Building	Washington, D.C.	OF	149.70	1.68	71.29	14.11	April 1, 2017
November	WBCMT 2007-C34	2007	Ashford Hospitality Pool 5	Various	LO	148.82	1.78	79.93	20.14	April 11, 2017
February	CSMC 2006-C5	2006	HGSI Headquarters	Rockville, Md.	OF	138.75	2.21	59.10	23.30	Sept. 1, 2016
December	COMM 2013-LC6	2013	540 West Madison Street	Chicago	OF	135.00	1.61	63.50	15.01	Jan. 6, 2018
November	WFCM 2010-C1	2010	Dividend Capital Portfolio	Various	MU	124.21	2.87	46.58	28.97	July 1, 2020
June	GSMS 2007-GG10	2007	55 Railroad Avenue	Greenwich, Conn.	OF	124.00	0.85	80.00	7.35	June 6, 2017
November	WBCMT 2007-C31	2007	Ashford Hospitality Pool 2	Various	LO	119.04	2.03	80.19	18.37	April 11, 2017
February	MSC 2006-IQ12	2006	Oxford Centre	Pittsburgh	OF	118.00	1.68	79.70	11.40	Dec. 1, 2016
March	GSMS 2011-GC5	2011	Copper Beech Portfolio	Various	MF	111.90	1.48	68.29	12.01	June 6, 2016
November	MSC 2008-T29	2008	Kimco Portfolio	Various	RT	109.27	1.27	66.70	14.19	Dec. 1, 2017
November	WBCMT 2007-C31	2007	Ashford Hospitality Pool 1	Various	LO	108.81	2.28	79.45	18.85	April 11, 2017
June	WBCMT 2007-C32	2007	Ashford Hospitality Pool 4	Various	LO	98.42	1.95	74.27	14.54	April 11, 2017
August	UBS 2012-C1	2012	Apache Mall	Rochester, Minn.	RT	93.16	1.74	66.58	10.35	Aug. 6, 2017
July	CSMC 2007-C1	2007	HGA Portfolio	Various	MF	92.48	1.93	79.90	12.24	Nov. 11, 2016
October	MSC 2007-IQ16	2007	USFS Industrial Portfolio Roll-Up	Various	IN	89.75	1.67	75.00	50.96	Aug. 1, 2017
November	COMM 2007-C9	2007	USFS Industrial Portfolio	Various	MU	89.75	8.90	75.00	50.96	Aug. 1, 2017
April	GSMS 2007-GG10	2007	915 Wilshire Boulevard	Los Angeles	OF	85.00	1.24	72.65	6.35	March 6, 2017
December	WFRBS 2011-C2	2011	Rentar Plaza	Middle Village, N.Y.	MU	76.83	2.23	52.10	13.48	Jan. 1, 2021
June	WFRBS 2013-UBS1	2013	Sullivan Center	Chicago	MU	75.00	5.10	49.60	15.31	Nov. 6, 2018
October	MSC 2007-T27	2007	Plaza at Landmark	Alexandria, Va.	RT	69.00	1.71	61.90	6.57	May 1, 2017
July	BSCMS 2007-T26	2007	Academy Sports HQ	Katy, Texas	IN	68.25	2.22	66.00	8.61	Feb. 1, 2017
September	GSMS 2013-GC16	2013	Matrix MHC Portfolio	Various	MH	67.96	1.63	69.40	16.19	Aug. 6, 2018
June	WBCMT 2007-33	2007	84 Lumber Industrial Pool	Various	IN	67.92	1.87	68.54	18.86	May 5, 2017
October	WBCMT 2007-32	2007	60 Madison Avenue	New York City	OF	66.50	1.21	79.17	4.69	May 11, 2017
August	WFRBS 2013-C17	2013	Matrix MHC Portfolio	Various	MH	64.10	1.63	69.40	16.19	Aug. 6, 2018
September	CGCMT 2007-C6	2007	Culver Center	Culver City, Calif.	RT	64.00	1.65	80.00	5.97	May 6, 2017
February	BSCMS 2006-PW13	2006	Fairmont Plaza Office	San Jose, Calif.	OF	60.12	1.53	73.60	6.97	June 1, 2016

Source: Trepp LLC

The Data Digest

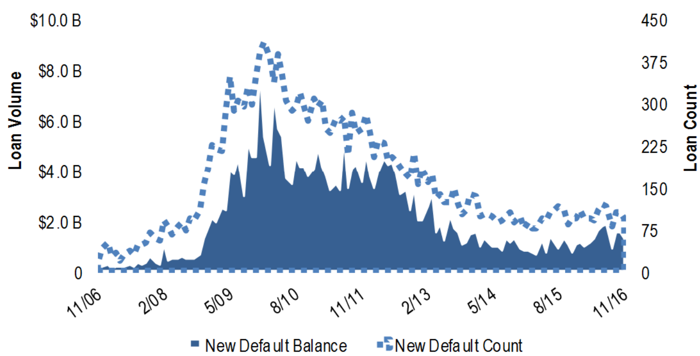
Special Servicer Volume



Source: Trepp LLC

The volume of CMBS loans in special servicing last year consistently remained at less than $30 billion. It was the first year since 2008 that monthly volumes remained below that level. But the volume of nonperforming loans in special servicing has steadily increased, to $22.1 billion, or 79 percent of the total in special servicing. The remainder is comprised of performing loans.

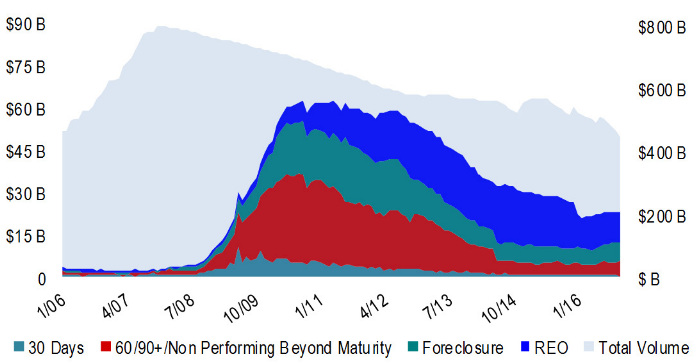
Monthly New Defaults



Source: Trepp LLC

An average of 100 CMBS loans defaulted every month last year, up from the average of just more than 93 that defaulted monthly in 2015 and 97 in 2014. A total of $14.9 billion of loans defaulted last year through November, up from $11.6 billion in 2015 and $13.2 billion in 2014.

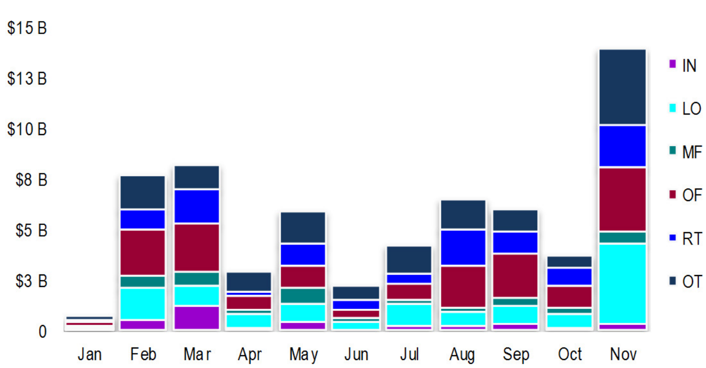
Delinquency Breakdown



Source: Trepp LLC

The volume of delinquent CMBS loans remained in a band between $21 billion and $23.3 billion throughout last year. But because new issuance hasn't kept up with the natural runoff of existing loans, the delinquency rate has inched up and is now just more than 5 percent.

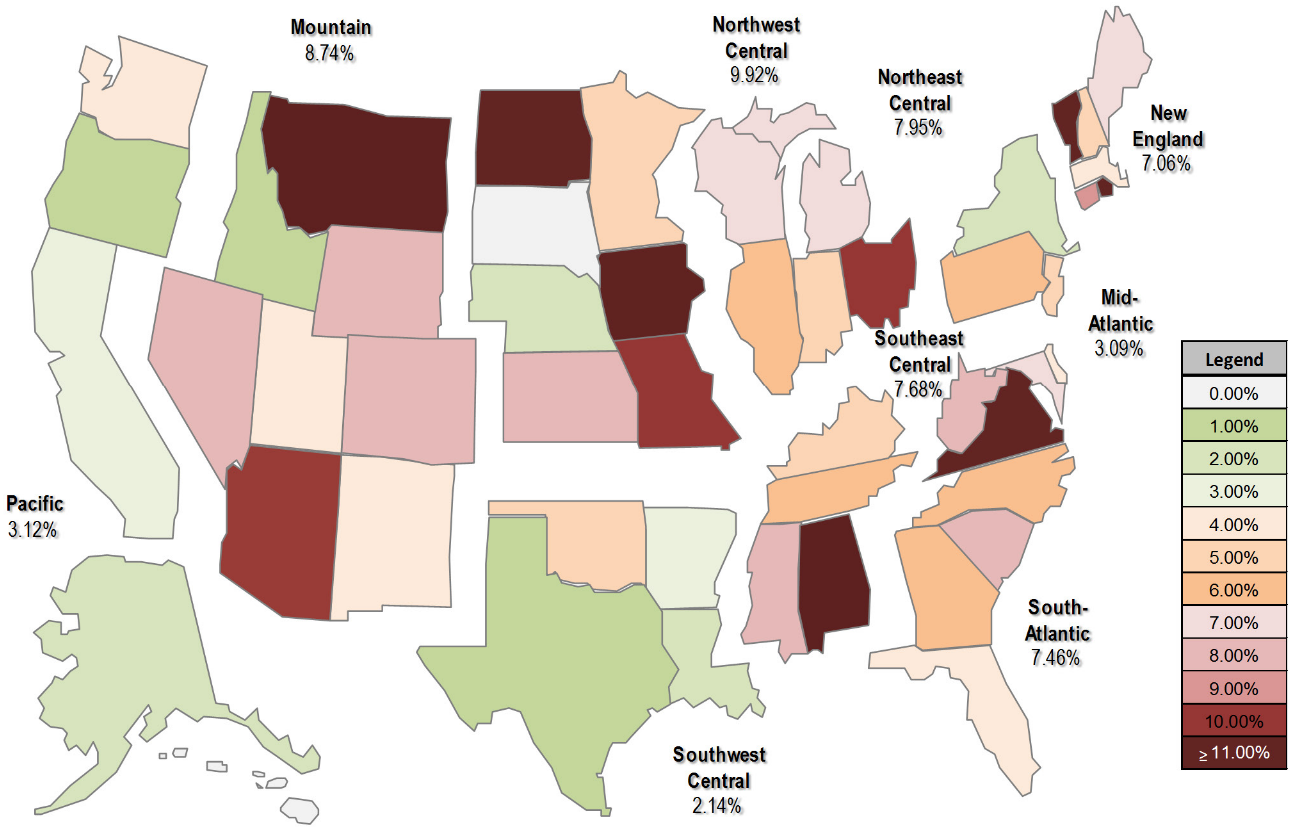
2016 CMBS Issuance



Source: Trepp LLC

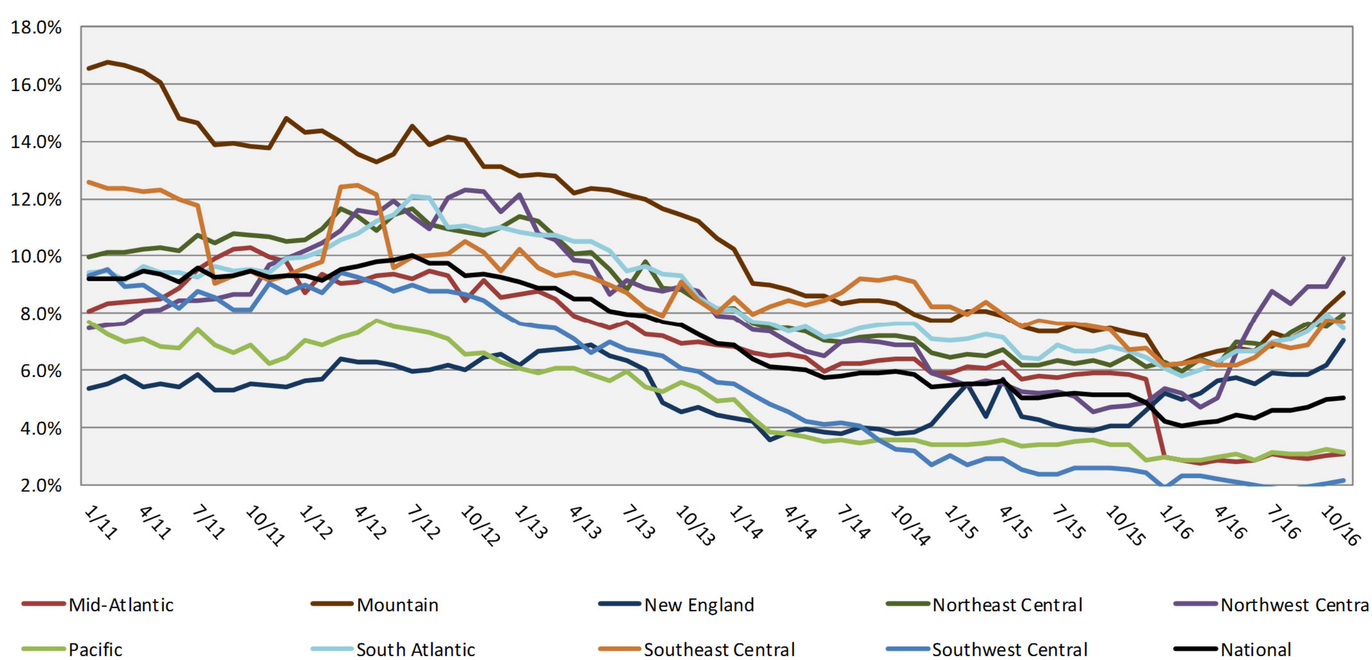
November was by far the most active month in CMBS last year, with $11.8 billion of new issuance, or more than 17 percent of the year's total. Office loans comprised more than a quarter of the collateral for the year's deals, with hotels comprising nearly 20 percent and retail totaling 18 percent.

Delinquencies by State



Source: Trepp LLC

Delinquencies by Region



Source: Trepp LLC

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