Commercial RealEstate Direct

THE YEAR-END

2017

AN EPIC TUG-OF-WAR IN THE RETAIL WORLD

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INSIDE THE YEAR-END

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LETTER FROM THE EDITOR

Orest Mandzy
Managing Editor

Last year could have been a disaster for the CMBS market. While it dodged the risk-retention bullet, it's now facing headaches of a different sort, namely the potential weak performance of retail loans.

Risk-retention rules, which went into effect in late 2016, were feared to wreak havoc on the market. Many were concerned that investors would be hard pressed to come up with sufficient long-term capital to take down enough subordinate bonds to keep the market relevant.

But they came through. And private-label CMBS issuance topped $86 billion, exceeding 2016 volumes by more than 26 percent. Perhaps more impressive was the fact that 18 investors took down risk-retention pieces from 65 transactions. That doesn't include the vertical slices that issuers retained from 56 deals.

Meanwhile, the fickle retail sector has put dozens of properties at risk. Shopping malls, once the darlings of developers and lenders, are now being avoided by most. While consumers continue to buy stuff, they're changing the way they do it. It's already having an impact on the CMBS sector and promises to keep industry players on their toes.

In the following pages, we've put together a series of articles in an effort to shine the light on the challenges the retail property sector is facing. Amazon.com is not the cause of all the sector's ills. Our expectation is that, just like it did with the risk-retention issue, the commercial real estate sector will figure things out. But it might take some time and cause some pain.

As we've previously done, we've included insight from several industry leaders. BuildFax, for instance, found that the issuance of retail permits is actually up, while project abandonment is down. Who would have figured that could happen given the black eye on the sector?

And EDR Insight found that despite all the negative headlines surrounding retail, 5,500 stores were slated to open last year.

We've also included our Year-End CMBS Awards — our league tables — in which we rank bookrunners, loan contributors, servicers and B-piece buyers. Tops in the bookrunner race was Goldman Sachs, which took a 13.4 percent share of the market. Its activity was driven by its dominance in the large-loan sector. Overall, it contributed $11.7 billion of loans to various deals. That accounted for 13.6 percent of all securitized loans.

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

E-Commerce: From Zero to 35 Percent of Retail Sales in 30 Years

By Tim Casey

When Amazon.com launched in 1995, the company focused on selling books online, a tiny niche that barely caught the attention of the retail industry. Today, the online retailer has become the largest e-commerce company in the world and has helped usher in an era where traditional retailers have invested more time and money into their online sales strategies.

During the first three quarters of 2017, e-commerce retail sales increased 15.6 percent from a year earlier to $333.1 billion, according to U.S. Census Bureau data. Total retail sales, meanwhile, increased 4.5 percent to $3.77 billion during that period.

Although e-commerce accounted for only 8.8 percent of sales in those three quarters, the percentage has steadily grown. For instance, it accounted for 8 percent of sales last year, 7.2 percent in 2015 and 4.8 percent in 2011.

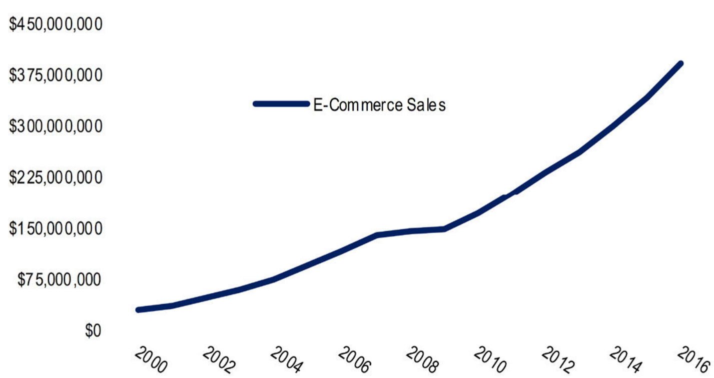
But the Census Bureau data underestimates the impact of e-commerce because it includes in total sales categories such as food, alcohol, automobiles and gasoline that are not usually or can't be sold online.

MetLife Investment Management estimates that if those categories are excluded, e-commerce accounts for 14 percent of sales. The company projects that e-commerce could grow to 30 to 35 percent of sales within the next decade.

E-Commerce's Origins

Online retail began taking off in the late 1990s, when investors poured money into Internet companies that sold goods such as books, clothing, toys, electronics, groceries and even pet food. Although e-commerce only accounted for 0.9 percent of retail sales in 2000, many investors were bullish on the prospect of online services becoming legitimate competitors to traditional brick-and-mortar stores. But by the early 2000s, many online retailers had filed for bankruptcy.

U.S. E-Commerce Sales



Source: U.S. Census Bureau

Top U.S. E-Commerce Companies - 2015 Data

Company	Sales ($bln)	% of Retail Revenue
Amazon.com	79.27	100.00
Apple	24.37	46.50
Walmart	13.70	2.80
Liberty Interactive	5.15	51.50
Macy's	4.85	17.90
The Home Depot	4.69	5.30
Best Buy	4.00	10.10
Costco	3.50	3.00
Nordstrom	2.83	20.10
Kohl's	2.80	14.60

Source: National Retail Federation

Still, e-commerce continued to grow each year, reaching 4 percent of retail sales in 2009. At the same time, traditional retailers weren't investing in their online platforms and, as such, faced challenges attracting computer engineers and developers who were more inclined to work for Internet-only retailers, such as Amazon.

"I don't think anyone predicted the wave of online acceptance to the level it is now and is becoming," said Byron Carlock, the head of PwC's real estate practice and former chief executive and president of CNL Lifestyle Properties Inc. "The obsolescence in retail has sped up in the last several years. Retailers are having to work hard to catch up to keep their customer, know their customer and serve their customer."

Department stores, in particular, have faced the challenging retail environment by cutting costs and reducing their workforces. In 2016, there were 25 percent fewer department store employees than in 2001, according to the Bureau of Labor Statistics.

"I don't think they fully understood the nature of the threat that they were facing," explained Adam Ruggiero, head of real estate research at MetLife Investment. The cuts "led to a deteriorating customer experience, which was actually their primary mode of defense against online retail — creating a strong, in-person customer experience."

Retailers Start Taking E-Commerce More Seriously

The approach has changed in recent years, as retailers have adopted so-called omnichannel strategies, where they offer goods to customers in stores, online through their websites and on their mobile-phone applications.

Today, traditional brick-and-mortar retailers Walmart, Target, Kohl's, Gap, Macy's, Apple, Costco and Nordstrom are among the 10 most-active online retailers, according to the National Retail Federation. The other two — Amazon

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The U.S. Shopping Mall - A Dying Breed?

By Jen Loukedis

If you've paid attention to recent headlines, you might think the mall is dying, if not dead already. Once a post-war mecca to suburban sprawl, the enclosed mall has seen its share of distress over the past few years.

As technology and changing consumer preferences have transformed the retail landscape, the mall has faced challenges. Anchor retailers like Macy's, Sears and JCPenney have dragged the mall as a category down with them. Some malls are not going to survive. Of the roughly 1,100 enclosed malls in the United States, up to 25 percent could close by 2021, according to a projection by Credit Suisse.

However, some malls are thriving.

Simon Property Group just completed an expansion of the King of Prussia Mall in suburban Philadelphia that added 155,000 square feet to the already mammoth property, making it the largest in the U.S. The mall's inline stores generate an estimated $975/sf in annual sales, which also makes it among the country's most successful properties, according to estimates by Green Street Advisors. It pegs Bal Harbour Shops in Bal Harbour, Fla., with an impressive $3,185/sf in sales, as the most successful in the country — and it doesn't even have an Apple store. The 450,000-sf property is owned by Whitman Family Development of Miami.

The number of shopping malls in the country increased five-fold, to 1,500, between 1970 and 2012, according to the International Council of Shopping Centers. Space dedicated to retail has grown by 400 percent since 1970, while the U.S. population has increased by only 50 percent, according to GGP Inc.

The U.S. has 23.5 sf of retail space per person, the most for any country, according to Morningstar Credit Ratings. That compares with 16.4 sf in Canada and 11.1 sf in Australia.

The enclosed mall was born of post-war expansion (*see centerfold*). Rapid suburban sprawl created the need for a place for people to congregate and shop. Favorable tax laws encouraged development and a growing interstate system provided the means for consumers to travel.

With money in their pockets and optimism in their hearts, consumers welcomed this new form of retail property with open arms. Malls also thrived because they faced little

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and Liberty Interactive Corp., which owns the QVC shopping network and its website — have little brick-and-mortar presence.

Meanwhile, many traditional brick-and-mortar retailers are using their stores as fulfillment centers, where customers can pick up and return items that they ordered online. At the same time, they're collecting customers' e-mail addresses in order to provide future incentives and advertisements.

"The direct online communication is a new retail phenomenon that says we know you, we know what you like to buy and you get to choose whether you want it online or in store," PwC's Carlock said. "All of a sudden your decision gets easier and easier as that relationship gets deeper and deeper."

Internet retailers, meanwhile, are starting to open stores to showcase their offerings, interact with customers and increase their brand awareness. Amazon, for instance, has opened 13 book stores in California, Illinois, Massachusetts, New Jersey, New York, Oregon and Washington, where it sells books and devices. It also has a partnership with Kohl's, in which Amazon customers can return items in 82 Kohl's stores in the Los Angeles and Chicago areas. Kohl's employees pack and ship the items to Amazon.

Online retailers "want you to also feel like you're part of the family for an in-store experience if you choose to have one," Carlock said. "That idea of having some brick-and-mortar exposure for their brand is helpful … and builds the relationship with you."

Growth in High-Speed Internet Availability Makes E-Commerce More Accessible

Of course, the growth in e-commerce wouldn't be possible without high-speed Internet access. In 2016, 73 percent of U.S. adults had high-speed broadband service at home, up from 61 percent in 2010 and only 1 percent in 2000, according to the Pew Research Center. In addition, 88 percent of U.S. adults used the Internet last year compared with 76 percent in 2010 and 52 percent in 2000. Furthermore, 77 percent of U.S. adults last year had a smartphone, making it easy for them to access the Internet anywhere and shop online.

Meanwhile, last year through November, 6,885 stores shut their doors — a 224 percent increase from the same period a year earlier, according to think tank Fung Global Retail & Technology. But at the same time, 3,427 stores were opened, up 49 percent.

Electronics retailer RadioShack, shoe store Payless ShoeSource Inc. and department store Sears were among the top five retailers to announce they would close stores. MetLife Investment's Ruggiero said certain retail categories — electronics, commodity apparel, men's clothing — are particularly vulnerable to e-commerce competition.

He added that other segments such as women's clothing and high-end goods still benefit from in-store sales. Luxury retailers, for instance, offer personal shoppers and the ability to touch and feel high-end items — that can't be done with an online retailer.

Discount retailers also are faring well. Dollar General, Dollar Tree, Aldi, TJ Maxx and Five Below were the top five retailers in terms of store openings in 2017.

While some online retailers have made efforts to sell food, the vast majority of food, alcohol and grocery items are still bought in brick-and-mortar stores.

Ruggiero said Amazon bought Whole Foods Market to improve its grocery sales, learn the business and gain access to valuable space. He speculated that Amazon could re-configure Whole Foods locations and convert some of the shopping space into warehouse space to facilitate delivery of goods.

"E-commerce has had a tremendous run over the last couple of years, and I think it's going to continue to have a great run," Ruggiero said. "But there's a lot of nuance into how each individual segment of retail is going to react to it." ■

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competition. Neighborhoods that sprang up out of former farm land did not, by and large, have central shopping districts.

But times have changed. The same phenomenon that helped create the mall — large-scale shifting consumer demographics — is what's responsible for challenging its existence today. While the Greatest Generation moved to the suburbs, Millennials are moving back to the cities and e-commerce has redefined how consumers shop.

But consumers are still shopping. Online spending last Black Friday, traditionally the busiest day for retailers, was a record $5.03 billion, up 16.9 percent over the previous year, according to Adobe Systems Inc. However, traffic in brick-and-mortar stores this past Black Friday was down 4 to 6 percent, according to an estimate by Cowen & Co.

So, it's no surprise that some traditional retailers are drowning. Apparel, a category that long was thought to be immune from e-commerce competitors, and shoe stores led the pack of store closures in 2017 with 1,483 in total, according to research from JLL. However, other retailers are thriving. JLL reports that 1,650 dollar stores opened last year.

What Makes A "Good Mall?"

Which qualities ensure a mall will survive and which are precursors to its demise? According to mall pioneer and developer Alfred Taubman, who died two years ago, it all comes down to design. A well-designed mall will break down the barriers between the customer and the merchandise, which he called "threshold resistance." The six pillars of smart design are convenience, a diverse mix of tenants, the feeling of luxury, differentiation, entertainment and comfort.

But smart design two decades ago might not be smart design today. Mall owners need to adapt to changing consumer preferences in order to stay relevant. The life expectancy of a mall is about 25 to 30 years, according to Ellen Dunham-Jones, author of "Retrofitting Suburbia" and a professor of architecture at the Georgia Institute of Technology. Mall construction reached its peak in the 1990s with the opening of 19 malls in the U.S., so it's no surprise that we're in a period of attrition.

Change requires capital. That puts the best-capitalized mall REITs at a point of advantage. They typically have better access to capital than other owners.

For instance, GGP invested about $700 million on renovations last year. In last year's third quarter, it had reported a 2.1 percent increase in inline store sales from the year before.

Taubman Centers, another owner of top-tier malls, has developed, renovated or expanded more than 75 percent of its properties since 2008. Inline sales for the firm climbed by 2.8 percent from a year earlier.

And Simon is retooling its tenant mix. Leases devoted to apparel retailers last year were down about 20 percent, and the percentage of leases signed with retailers devoted to food and entertainment was up about 20 percent. The Indianapolis company also has a team dedicated to up-and-coming retailers that may have started with digital-only platforms, but might be interested in expanding to physical stores. Many of these retailers, like Bonobos, open mall stores that function as showrooms, so they require smaller footprints than traditional retailers.

Macerich Co. is also eying digital retailers, and has put together a list of more than 400 that could be candidates for space at its malls. To entice them, it's considering flexible short-term leases.

GGP, meanwhile, is looking to revamp some of its malls, effectively turning them into mixed-use properties. It added the Park Lane at Ala Moana residential condominiums to its Ala Moana Center in Honolulu. Open since April, the project is 95 percent sold. It's also signed an agreement with AvalonBay Communities to develop a residential component to a GGP retail center in Seattle.

As willing as they are to upgrade and evolve profitable malls, the top mall REITs are equally willing to let go of underperforming ones. So, ownership is a function of profitability as much as it is a product of it.

Struggling Malls Cannot Find Their Way

Meanwhile, it's harder for struggling malls to turn around, as their declining economics make it difficult to attract capital.

Green Street estimates that 300 malls in the country have inline store sales between $250/sf and $324/sf. Many of those are anchored by Sears, JCPenney and Macy's, and they're at most risk of closing. They collectively represent roughly 5 percent of the value of the entire U.S. mall universe.

Moody's Investors Service recently noted that malls with inline sales of less than $400/sf are facing the most pronounced risk.

In contrast, roughly 300 malls in the country generate inline store sales of $500/sf or more, according to Green Street. They've doubled in value since the Great Financial Crisis.

But second-tier malls still have a place in the retail landscape. In a 2016 survey by Westfield Corp., 45 percent of U.S. shoppers ranked the traditional mall as their preferred retail destination. Of course, Westfield itself is a mall owner and developer.

While e-commerce is important, it's only part of the retail puzzle. Being omnichannel — that is, successfully spanning physical, mobile and social platforms — is where retail has headed.

A 2016 study of Millennials by CBRE found that 70 percent of the shopping that 19- to 34-year-olds do is conducted in physical stores. Even more encouraging is that 56 percent of this age group likes the experience of seeing a product in real life before buying.

But it gets better. Generation Z, comprised of those born after 1995 and which totals 26 percent of the U.S. population, is expected to generate $44 billion in annual spending, according to a 2017 survey from IBM and the National Retail Federation.

This complex group has never known a world without smartphones or other digital technology. However, the survey found that 67 percent of the Gen-Z group actually prefers shopping at brick-and-mortar stores most of the time and 31 percent prefer in-store shopping sometimes. But they want technology to seamlessly integrate with their store shopping experience and interactive engagement around their brands.

In the retail jungle, the strongest malls will not only survive, but thrive. Some of the others will be lost due to a number of circumstances, such as location and lack of access to capital. Many of those might find new lives as mixed-use developments or, the ultimate irony, as distribution centers for e-commerce retailers. ■

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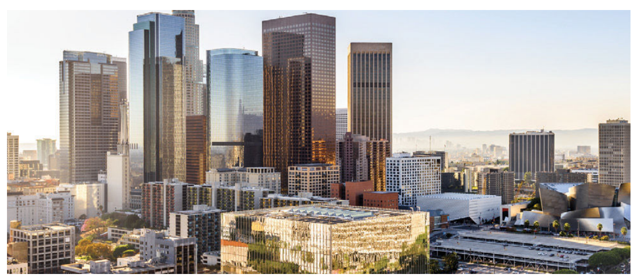

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Hotel Sector Remained Resilient Last Year, But Supply Should Pressure Metrics in 2018

By Jenny Robinson

Hotel performance in the United States is still in the positive column, with occupancy and room rates both increasing last year.

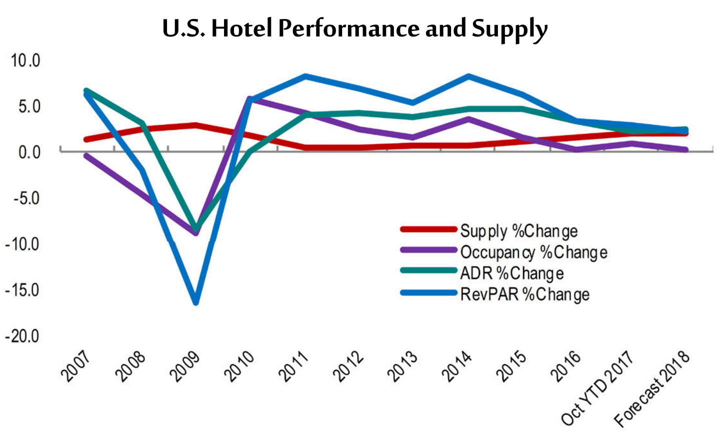
But continued increases in supply will pressure occupancy, resulting in a slowing of revenue growth.

Hotel occupancy last year increased by 50 basis points to 65.7 percent, according to STR. That was substantially better than what had been expected — STR anticipated a 30-bp drop in occupancy. But the 2.1 percent increase in room rates, to $126.66, was less than the 2.8 percent increase that had been projected. Revenue per available room increased by 2.5 percent.

For this year, the Hendersonville, Tenn., research firm is projecting a 20-bp drop in occupancy, to 65.6 percent, and a 2.4 percent increase in rates, for a 2.2 percent increase in RevPAR to $85.06.

"We're really at the top" of the cycle, explained J.P. Ford, senior vice president and director of business development at Lodging Econometrics. "We're just bouncing along the top. No big declines, no big increases ... There's nothing really on the horizon that says we're in for a big downturn."

Wells Fargo Securities recently noted that 2017 might have been the year in which hotel performance growth plateaued. It says "hotel revenue growth is steadily descending."



Source: STR Inc.

STR's forecast for this year assumed that tax legislation gets signed and the country continues to enjoy economic growth.

The tax cuts in the legislation could generate $131.7 billion of economic activity for hotels and related industries over the next 10 years, according to the American Hotel & Lodging Association.

Meanwhile, hotel fundamentals remain closely tied to general economic conditions. As the economy grows, so does demand for hotel rooms. Normally, as demand increases, the ability for hotel owners to increase room rates improves. But that hasn't happened as "hoteliers just feel uncertain about the future," explained Jan Freitag, senior vice president of Lodging Insights at STR. "They're not sure how long the growth can last."

Hotel operators, meanwhile, have faced an increase in supply, but growth also has moderated.

STR reported that 183,187 rooms are under construction nationally, a 10-bp drop from the previous year.

In New York City, 12,702 rooms were under construction as of October, far more than any other city. But the figure is 23 percent lower than the 16,546 rooms that were under construction a year earlier.

"There is a tapering of new additions to the pipeline," explained Lodging Econometrics' Ford. "It's still growing, but at a decelerating rate. We're not seeing 200-300 projects added to the pipeline on a quarterly basis."

Nonetheless, heavy new supply continues to plague certain markets. New York City and Miami are both expected to see drops of 5 percent or more in RevPAR. Both saw their supply of rooms increase by about 4 percent last year, more than double the 1.9 percent increase in supply nationwide.

Nashville, Tenn., is another market that has seen a big increase in supply, with 5,472 rooms in its construction pipeline last year, up 67.5 percent from 2016. The result: a 50-bp drop in occupancy from the previous year.

Upscale and upper-midscale limited-service brands such as Courtyard and Hilton Garden Inn continue to dominate construction financing and development.

"I don't see that switching or changing any time soon," Ford explained. "In 2018, those brands will still be dominant in terms of additions to the pipeline and new openings."

The ability for homeowners and apartment tenants to lease their units on a short-term basis through booking sites such as Airbnb also is a growing threat to the hotel sector.

A Morgan Stanley survey found that a quarter of travelers used Airbnb in the past year, up from 22 percent in 2016, and 14 percent the year before that. According to a study by credit ratings agency DBRS, Airbnb's worldwide listings — 3 million — have surpassed the number of rooms offered by Hilton, Marriott and Wyndham combined.

And Airbnb rooms, on average, tend to cost less than hotels. In Dallas, for example, the average Airbnb room was listed for $69. That compares to the average hotel room's list price of $135. In Philadelphia, the Airbnb price was $61.18, which compares with the $183 hotel room price.

"Come 2018, Airbnb will likely be accommodating as many guest arrivals as some of the most well-known hotel brands in the industry unless regulation is passed to substantially modify the company's current business model," DBRS noted.

The American Hotel & Lodging Association already is lobbying toward that goal. The organization claimed a victory with a law in New York State that was signed in 2016, imposing fines on apartment dwellers who advertise their units for rentals of 30 days or less.

As if the hotel sector didn't face enough challenges, it's being hit by a decline in tourism. The U.S. Department of Commerce reported a 3.9 percent drop in international tourism for the first half of last year.

While 4.8 percent more Canadian tourists crossed the border to visit the lower 48 states than a year earlier, 9.4 percent fewer tourists from Mexico came north to visit. Visits from the United Kingdom, meanwhile, were down by 6.2 percent.

Apocalypse Not: Why The Demise of Retail Centers Is Some Truth, Some Hype

By Ryan Severino

One of the following two things is true: either people who work in commercial real estate are liars or they are the only people who do not go to malls.

Of course I am being a bit facetious, but at virtually every conference I attend or speak at, I inevitably hear someone say that malls are dead or, more broadly, that retail is dead. To be fair, real estate players are not alone. The term, "Retail Apocalypse" is now commonly used. Is that the truth or just hype? It's a bit of both, but leans mostly toward hype because this declaration of Armageddon paints the sector with a very broad brush across too many dimensions. By digging into what's behind the pessimism, we can see why some retail centers are struggling and others are thriving.

Why So Sad?

The reason for all the doom and gloom in retail real estate is e-commerce. E-commerce sales continue to grow far faster than overall sales. As of last year's third quarter, e-commerce was growing at a roughly 16-percent rate, while overall sales were growing at a roughly 4-percent rate. Official figures show that e-commerce constitutes about 9 percent of overall retail sales. But that understates the true percentage *(see story on page 4)*. On one hand, 9 percent is a minority of overall sales. On the other, even at just 9 percent, e-commerce has caused serious problems for some brick-and-mortar retail centers. Even if e-commerce sales growth slows from its blistering pace, it will continue to grow faster than overall sales and be increasingly disruptive to retailers.

Who Bears the Brunt?

Although e-commerce continues to grow, it's not impacting all retailers equally. Those most at risk are the purveyors of what can be thought of as commoditized goods. These are common, general goods that consumers are broadly familiar with. The imperiled retailers of such items generally fall into two categories: those that sell other producers' goods, and those that sell goods that do not have a moat — some brand loyalty or uniqueness that protects their business.

Consumers are increasingly willing to purchase commoditized goods online, which has been reflected in store closures. For example, the stores that have closed in recent quarters have been concentrated only in a few areas: apparel, shoe and department stores.

While department stores sell some items under their own labels, they overwhelmingly sell the goods of other producers. The same holds true for many general shoe stores. And even though many apparel retailers are selling their own brands, consumers often find them similar to other brands and not differentiated enough.

So, What Works?

At the other end of the spectrum, you'll find the sellers of goods that consumers cannot or will not purchase online.

These retailers aren't just surviving, they're thriving and opening stores. Wireless providers are faring well. While cell phones could, in one sense, be viewed as a commoditized product, people prefer to purchase them in stores because phones require the purchase of airtime and data plans, activation on a network and often the transfer of data stored on their current phones.

Dollar stores, convenience stores and discounters also continue to thrive because many of the things purchased in these stores are incredibly cheap and are difficult to sell online because inventory is idiosyncratic. For example, discounters receive excess inventory that other retailers failed to sell. Often this does not have a full size or style run (because some of it has been previously sold at another store). And, of course, grocery stores continue to sell goods that often have a short shelf life, that consumers want to physically inspect before purchasing and that they often need on relatively short notice. To a lesser extent, the same holds true for pharmacies and drug stores.

Evolving Consumer Preferences and Behaviors

Preferences and behaviors of consumers are also changing. Consumers are shifting away from purchasing goods and are increasingly purchasing services. Obviously, cell phones fall into this category, as they provide a service as much as a physical item. However, consumers also will spend money on experiences like dining out, getting a drink, going to the movies or playing games at venues like Dave & Busters.

These are experiences that cannot be fully replicated online, even if consumers spend a good part of their time at these establishments documenting their experiences on social media. Additionally, consumers continue to prefer goods that are unique or offer some sort of brand value to them. The rise of specialty retailers that produce in smaller quantities but offer unique, less common goods reflects this. And some brands (including apparel retailers) can thrive if their brands engender loyalty and value among dedicated consumers.

Don't Forget Economics

Because of the rise of online retailing and changing consumer preferences, retail is going through the next phase of its evolution. Those shopping centers that successfully execute on this evolution will succeed.

But economics still matter.

Thriving retail centers need to be supported by strong

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2017 Was Huge for Retailer Bankruptcies; CMBS Dodged a Bullet

By Karina Estrella

Last year, more than 30 U.S. retailers filed for bankruptcy protection.

While not necessarily indicating that the retail sector is weakening, the filings have had a substantial impact, not only on properties, but also CMBS, as more than $35 billion of securitized loans are exposed to at least one retailer on that list. The main culprit for what many call the brick-and-mortar "retail apocalypse" is the surging growth of e-commerce and transformed consumer trends.

Online shopping giant Amazon.com and other retailers with comparable digital platforms have proven that e-commerce can compete in virtually every corner of the retail industry. Consumers are turning online to buy apparel, home goods, shoes, electronics, sporting goods and even groceries. E-commerce demand began to skyrocket in early 2015, and has continued growing relentlessly as more and more retailers implement faster last-mile delivery services.

While Sears, Macy's and JCPenney weren't among the retailers that filed last year, the three department-store chains shuttered more than 500 stores. The popularity of traditional department stores is plunging, in step with the rise of e-commerce, and hundreds of malls nationwide report declining foot traffic. Consequently, retail CMBS loans secured by regional malls and shopping centers are those most vulnerable to the recent rounds of retail bankruptcies and store closings.

Part of the issue is that the country simply has too much retail space, including in malls. Between 1970 and 2015, the number of malls constructed outpaced growth in the general population. What's more, mall visits dropped by 50 percent between 2010 and 2013, according to Cushman & Wakefield.

Meanwhile, retail sales increased by 2.6 percent in 2016, and 5.6 percent during the first half of last year. The retailers that had filed for bankruptcy or were planning to shutter stores generally have failed to adapt to market trends.

Industry experts observe that many of the companies that declared bankruptcy are concentrated in a few highly competitive areas.

Leslie Hand, vice president of advisory IDC Retail Insights, observes, "the majority of weakness that we have seen is in apparel, footwear and related segments, consistent with our expectation that these segments are over-stored, overstocked and simply out of alignment with consumer share of wallet/spend."

Indeed, according to the U.S. Census Bureau, sales at clothing stores through last October were up only 0.6 percent from the same period a year earlier. At sporting goods, hobby and music stores, they were 4.5 percent below the year before, and at department stores, they were 2.8 percent lower.

Retailers specializing in those sectors form the backbone of malls. So many owners are increasingly focused on revamping their properties, particularly their better-performing malls and shedding weaker properties. They're also luring more food, entertainment, fitness and other specialty retailers that can adapt and incorporate experiential technology into their offerings.

Following is a list of some of the major retailers that filed for bankruptcy last year. It would be led by Toys "R" Us, but the company's filing was driven not so much by weak sales as it was a defensive maneuver to buy time to restructure its massive debt load. The retailer said the filing wouldn't affect operations in the United States, where it operates 885 stores, including its Babies "R" Us franchise.

The Limited

Once a popular working woman's clothing chain, The Limited declared bankruptcy in mid-January and was subsequently purchased by private-equity firm Sycamore Partners. The Ohio apparel company closed all 250 of its U.S. stores and sold off its e-commerce domain and brand name. The retailer later moved its entire inventory online, and relaunched its e-commerce site in late October. A total of $14.7 billion of CMBS loans have some exposure to the retailer, but the 127 loans typically are backed by large regional malls, where The Limited is a relatively small tenant.

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trade areas that boast not only a sufficient number of consumers to support them, but also the requisite income and wealth levels among those consumers. Centers with these characteristics boast full parking lots, ample foot traffic and long lines at their Starbucks locations.

Retail real estate has become a world of "haves and have-nots," and the rift between the two continues to widen. The have-nots will continue to struggle and face an uncertain future, with many not surviving. The haves will continue to offer goods and services that consumers stand ready, willing and able to purchase. So the next time you're waiting in a long line in a mall you will understand where everyone came from. Some of them might even be real estate players. ■

Ryan Severino is chief economist at JLL and oversees global and regional economic research, analysis and forecasting as well as property market forecasting.

Continued from previous page

Gymboree

Children's clothing company Gymboree filed for bankruptcy in mid-June, reporting about $1.4 billion in debt. Its aim is to close up to 450 of its 1,281 stores. The company buckled due to weakened sales, driven by competition from more-established retailers such as Children's Place and GapKids, as well as online retailers. E-commerce sales comprise 21 percent of Gymboree's revenue. The retailer occupies stores in properties that back 75 CMBS loans with a balance of $5.4 billion, but it's typically not a top tenant.

Payless ShoeSource

Discount footwear retailer Payless ShoeSource filed for bankruptcy last April and immediately shuttered 378 U.S. stores, which later increased to 700 stores. The company emerged from bankruptcy in August, with plans to expand its e-commerce platform. A total of 86 CMBS loans totaling $3.9 billion include Payless as a top-five tenant. But only 31 loans totaling $935.3 million have an exposure to stores that Payless is closing.

RadioShack

Longstanding electronics retailer RadioShack filed for bankruptcy in March, its second filing since February 2015. The retailer closed 1,000 stores by last summer, leaving only 70 stores open. Another 500 stores are owned by independent franchisees.

hhgregg

Appliance and electronics retailer hhgregg and its Gregg Appliances unit filed for bankruptcy protection in March, after struggling with declining sales for four years. The company was listed as a top tenant at properties backing 42 CMBS loans totaling $1.8 billion. A month after filing, the company said it would liquidate all 220 of its stores after having failed to find a buyer.

Rue21

Teen clothing store Rue21 announced in April that 400 of its 1,218 U.S. locations would close. Soon after, it filed for bankruptcy, citing "decreased sales and increased operating costs, the shift away from brick-and-mortar retail sales to online channels and the tightening of trade credit." The company emerged from bankruptcy in September with 758 stores and a de-leveraged balance sheet. CMBS exposure totals 66 loans with a balance of $1.7 billion. But the retailer typically occupied relatively small locations at sizable properties that serve as collateral.

Gordmans

Gordmans Stores Inc., an Omaha, Neb., department store company, filed for bankruptcy in March. The following month, it identified 48 of its 105 stores that would close and 57 that would continue operating as discount stores under the new ownership of Stage Stores, which paid $40 million for the stores, as well as an Omaha distribution facility. CMBS has an exposure to 28 properties totaling $944.3 million where Gordmans is a tenant. But only eight loans totaling $312.8 million are tied to stores earmarked for closure.

Gander Mountain

Outdoor goods retailer Gander Mountain Co. filed for bankruptcy in March and two months later was bought by Camping World Holdings Inc., which said it would re-brand most of Gander Mountain's stores as Gander Outdoors or Overton's stores. Some stores will shutter permanently. While a total of $432.6 million of CMBS loans have an exposure to the retailer, only five loans totaling $65.7 million will be impacted by the closures.

MC Sports

Grand Rapids, Mich., sporting goods chain MC Sports filed for bankruptcy in February, citing weak sales and increased competition. Ten CMBS loans totaling $417.2 million are exposed to the retailer. The company is closing all 68 of its stores.

BCBG Max Azria

Fashion retailer BCBG Max Azria Group also filed for bankruptcy in March. CMBS exposure to the retailer, which had operated 175 stores, was limited, with only $200 million of loans potentially affected. But a $35 million loan was liquidated in June, leaving only a $165 million exposure. Also that month, the bankruptcy court approved a sale of the company's intellectual property to Marquee Brands and inventory to Global Brands Group Holding, which will keep operating 22 stores.

Other retailers, including Styles for Less, Aerosoles, Perfumania, True Religion, Wet Seal and Alfred Angelo Bridal, also filed for bankruptcy. But they had no impact on CMBS. So while the retail sector was hit hard by bankruptcies in 2017, CMBS was well insulated.

That's not to say that mall-backed CMBS loans are out of the woods. While class-A malls continue to record improving sales figures, class-B and lesser malls remain challenged.

Owners of class-A malls have the luxury of being able to use cash flow their properties generate to improve them by adding dining and entertainment options and otherwise diversifying their tenant mixes.

Meanwhile, lesser malls, which often are anchored by middle-market department stores that also are struggling, will find it difficult to get redeveloped or improved. Many will likely follow the lead of other class-B malls that were lost to foreclosure and sold to opportunistic developers and entrepreneurial operators. ■

The Good, The Bad and The Ugly: 2017

By Manus Clancy

The term "winning ugly" was first coined in 1983 about the Chicago White Sox. The team would go on to capture the American League West — the ChiSox' first title of any kind since reaching the World Series in 1959. The term became a rallying cry for the franchise after the manager of a rival team claimed the Pale Hose weren't really playing good baseball — they were winning ugly.

That term could have been applied to the financial markets in 2017. There was plenty that could have roiled them over the last 12 months — from North Korea, to uncertainty (as usual) in the Middle East, to gridlock (again) in Congress, to worries over asset valuations and interest rates.

But investors throughout the year overlooked the potential risks and continued to drive many markets higher — in many cases, to all-time highs. Talk about Winning Ugly.

Good Headlines from 2017

- **January**: Clemson upsets Alabama to win NCAA football title with last second touchdown.
- **January**: First post risk-retention CMBS deal is priced at impressively tight levels, setting tone for rest of 2017.
- **April**: HSBC renews lease for 500,000 square feet of Fifth Avenue (N.Y.) space behind single asset deal.
- **July**: Atlanta Property Group purchases six office buildings behind $129.7 million 2013 SOP Portfolio loan, securitized through UBSBB 2013-C5.
- **July**: Trepp CMBS Delinquency Rate begins to fall as Wall of Maturities nears completion.
- **August**: Northern Trust signs on for 462,000 square feet of space at 333 South Wabash Ave. in Chicago.
- **October**: CMBS rallies anew; long AAA prints at S+76 — among the highest levels of the year.
- **November**: Weeks after Hurricane Harvey pum mels southeastern Texas, Houston Astros win their first World Series title.
- **December:** CMBS issuance remains strong even post Thanksgiving as 2017 issuance total hits $86.4 billion.

Bad Headlines from 2017

- **January:** Sears and Macy's announce a new round of store closings within days of each other.
- **February**: Eastern Outfitters, owner of Bob's Stores and Eastern Mountain Sports, files for Chapter 11 bankruptcy.
- **February/March**: MC Sports, Gander Mountain, hhgregg and Gordmans file for bankruptcy.
- **March**: $112 million loan against One AT&T Center in St. Louis sent to special servicing.
- **June**: Sears announces it will be closing an additional 72 stores.
- **June**: Amazon.com buys Whole Foods — CMBS investors worry the online retailer will swallow everyone.
- **June**: Federal Reserve Board raises rates for second time in 2017.
- **August**: Value of 545 Long Wharf Drive in New Haven, Conn., which backs a $28.6 million CMBX 6 loan, cut by nearly 80 percent.
- **September**: Three CMBX 6 retail loans, with a total balance of $240.7 million, sent to special servicing on same day. CMBX spreads widen.
- **October**: Toys "R" Us files for Chapter 11 bankruptcy.
- **November**: Bon-Ton announces it will be closing 40 stores.

For the commercial real estate markets, there was plenty to worry about. Many of those concerns came from the retail space as worries about department stores, in-line retailers, sporting goods operators and grocers led to endless hand-wringing. While that was the biggest concern, it was not the only one: worries about hotel and multifamily properties in some markets and the obsolescence of some suburban properties also kept some of us up at night.

Yet, in the end, it was a "winning" year for the CMBS market. The combination of tight supply, the appeal to investors of risk-retention structures, extremely low volatility, and ongoing low interest rates made for a banner year for issuers. ■

Ugly Headlines from 2017

- **February**: Atlanta Falcons blow 28-3, third-quarter lead in Super Bowl, "losing ugly" to the New England Patriots.
- **April**: Loan against UBS Center in Stamford, Conn., resolved with $112 million loss.
- **July**: Value of former OfficeMax headquarters in Naperville, Ill., cut by almost 85 percent.
- **October**: Hurricane Maria wreaks havoc in Puerto Rico and Florida.
- **November**: Loan against 400 Atlantic in Stamford, Conn., resolved with $165.8 million loss.

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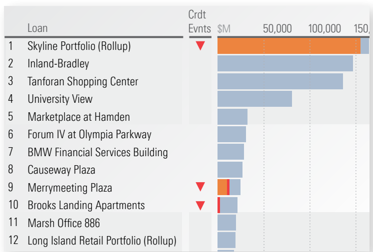
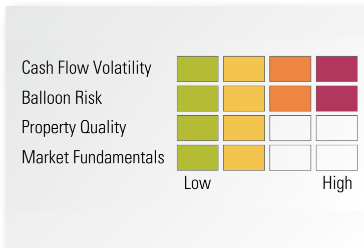


Projected losses and credit event indicators



Analyst perspective on critical risk factors

Method	Likely	Bearish
Appraisal	65,500	
DCF	**54,650**	**42,500**
Income Approach	57,100	
Value Deficiency		315
Loss	0	315
($000)		

Likely and bearish valuations and losses

DealView® CMBS Monitoring provides investors with Morningstar's insightful perspective and opinion on credit risk, with new proprietary valuations and loss analytics.

Enhanced Content

- In-depth real estate analysis including multiple property valuations and a Morningstar concluded value, with likely and bearish projected loss scenarios
- New proprietary risk and performance measurements including Morningstar's Loan Risk Score, Loan Hazard Meter, and Maturity Risk Heat Map
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- We encourage investors to talk with our analysts to discuss our credit approach and conclusions
- Our team of experienced analysts has a deep understanding of commercial real estate, structured finance, credit modeling and fundamental credit analysis
- We developed our analysis with CMBS investors to ensure its content and presentation efficiently address credit issues most important to investors

Improved Accessibility

- Functional navigation allows for quick access to related information throughout
- Morningstar's DealView CMBS Monitoring and proprietary loan analytics are available via an application program programming interface (API), feeds, and an excel add-in for integration with third party models and applications
- Subscribers can access via Trepp and other third party platforms

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It’s Not All Doom and Gloom for Retail in the U.S.

By Holly Tachovsky

Does this sound familiar? “Online sales are killing brick-and-mortar retail.” It’s a popular sentiment, with some predicting the demise of brick-and-mortar retail and the ongoing shuttering of malls and shops.

Despite the headlines, brick-and-mortar retail locations have been buzzing with construction activity. So, what’s really going on?

New research from BuildFax examines nearly 17 years of construction data on retail structures in the United States. Here’s how it all plays out.

Figure 1 : U.S. Retail Permit Issuance

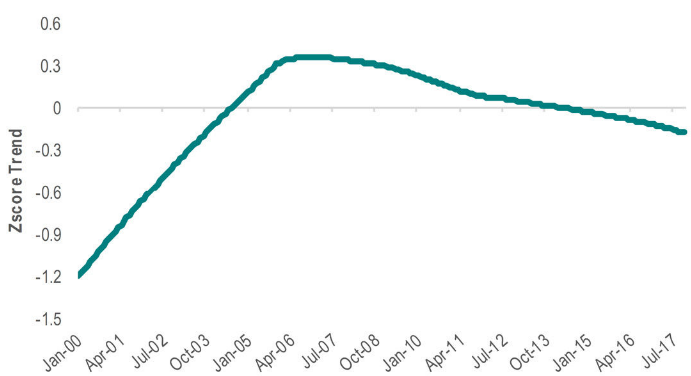
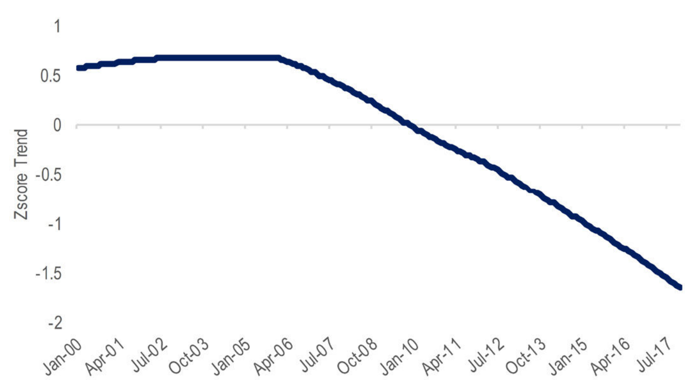


Figure 2: U.S. Retail Permit Abandonment



Figures 1 and 2 were plotted using z scores to provide a sense of overall changes over time.
Source: BuildFax

Retail Permit Issuance and Project Abandonment – Overview

When looking at retail permit issuance and project abandonment from 2000 to 2017, one overall trend is evident: issuance is outpacing abandonment. Currently, more permits are being issued (Figure 1) and fewer projects are being abandoned (Figure 2).

The evidence suggests that, after recovering from the recession, retail construction activity remains healthy. Additionally, these results may also point toward a positive outlook for the economy. Since fewer projects are being left incomplete, there is likely more confidence in retail construction.

During the previous economic downturn, both permit issuance and abandonment experienced noticeable dips. Despite a slight downturn in the last few years, permit issuance appears to be on a steady plateau. Meanwhile, abandonment rates have plummeted to an unprecedented low.

Figure 3: Urban Retail Issued Projects vs. Abandoned Projects (2001-2017)

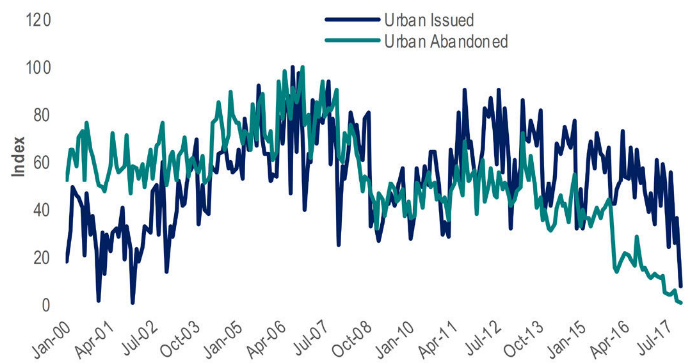
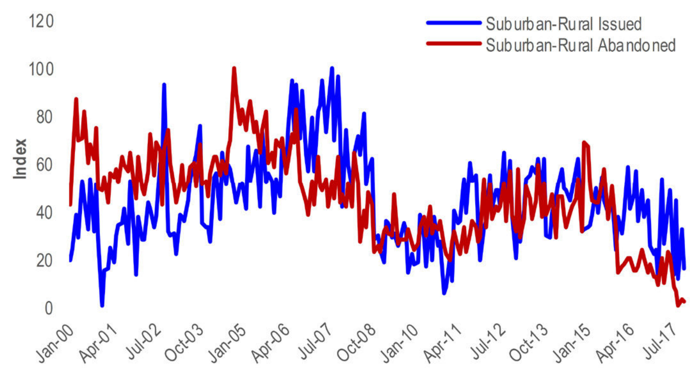


Figure 4: Suburban-Rural Retail Issued Projects vs. Abandoned Projects (2001-17)



Source: BuildFax

Urban vs. Suburban-Rural Retail

The plots above show issued and abandoned permits indexed to visualize the differences in their trends. Figure 3 illustrates urban retail issued projects versus abandoned projects; Figure 4 illustrates suburban-rural issued versus abandoned.

For both urban and suburban-rural retail permit activity, issuance is up over the last 17 years and abandonment is down. This mirrors the combined trends illustrated in Figures 1 and 2.

What Happened During the Great Recession?

Interestingly, for both urban and suburban-rural areas, a large gap existed between abandoned projects and issuance even before the economic crisis. There were considerably greater

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incidents of project abandonment than permit issuance.

Figure 3 shows that, except for a few brief convergences, the gap between abandonment and issuance persisted in urban areas until late 2013. In early 2015, the rate of abandonment dropped dramatically and reversed the trend. Currently, urban areas show a higher rate of issuance than abandonment.

Figure 4 illustrates a similar turnaround for suburban-rural areas in 2015. From 2006 to 2015, these areas saw rates of abandonment and issuance trending together. Similar to the reversal in urban areas in 2015, suburban-rural areas experienced a huge drop in abandonment that has persisted until today.

A Look at Volatility and What It Means

While issuance and abandonment trended similarly for urban and suburban-rural areas, there's one key differentiator to note in these data: greater volatility for urban retail permit activity, especially during the last five years. From 2012 to 2017, urban issuance was 30 percent more volatile than issuance in suburban-rural areas, whereas project abandonment shows about the same volatility in both geographies.

For urban areas, the volatility could be a sign of health, indicating a constant churn in retail construction; businesses are created, renovated, and destroyed with some regularity. It follows that densely populated, urban areas would generate a greater demand for retail space remodels to stay competitive. An example is the rise in popularity of pop-up shops, restaurants, and other limited engagement venues.

For suburban-rural areas, lower volatility indicates that not much is changing. Is it because there's not as much competition in these less-populated areas? Are shops choosing to forgo renovations as online shopping affects suburban-rural brick-and-mortar stores more than those in urban areas?

A Healthy Outlook for Retail Construction

Is retail headed for doom and gloom? No, the construction trends point to a different possibility.

Not only are fewer retail construction projects being abandoned, but in general, retail permit issuance is up nationwide. Additionally, greater volatility in urban areas suggests that retail construction is healthy due to consistent demand for renovations.

Considering the 2015 trend reversal in favor of issuance, the data suggest that perhaps the hype about retail's demise is unwarranted.

Key Takeaways

• Overall, retail permit issuance is up and abandonment is down. This points toward a favorable outlook for the economy.
• Retail permit abandonment is at an all-time low.
• In early 2015, for both urban and suburban-rural areas, the rate of abandonment dropped dramatically. This reversed the trend in favor of permit issuance rather than project abandonment.
• Urban areas experienced 30 percent greater volatility in retail permit issuance than suburban-rural areas from 2012-2017. This increased volatility may indicate urban retail health, as businesses are constantly being created, renovated and destroyed. ■

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

The CMBX Trade Against Retail: Has it Paid Off?

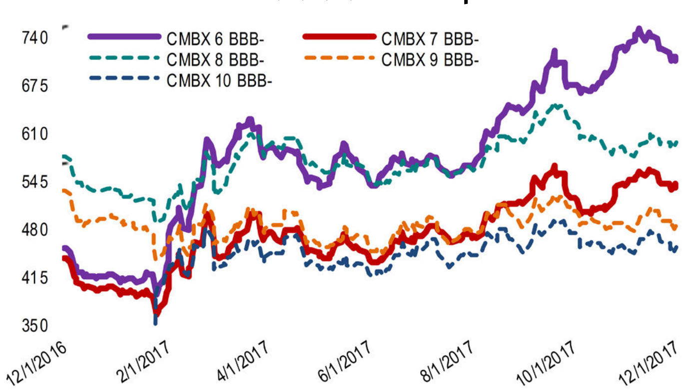
By Catherine Liu

Since early last year, a number of opportunistic investors have sought to profit from the expected demise of the physical retail sector.

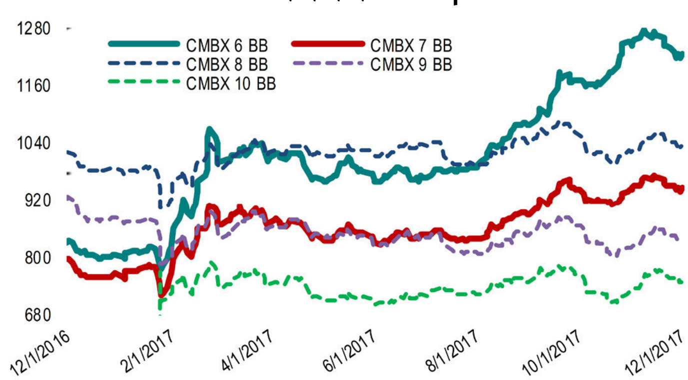
They invested in credit-default swaps against subordinate bonds in certain CMBX derivative indices that are tied to CMBS deals with healthy concentrations of loans against shopping malls and retail centers.

The trade gained notoriety last February, when spreads for the BBB- and BB rated components of the indices went through a massive widening. They continued to widen almost steadily until recently. That alone indicates the trade, particularly if executed early, has paid off nicely.

CMBX 6/7/8/9/10 BBB- Spreads



CMBX 6/7/8/9/10 BB Spreads



Source: Trepp LLC

CMBX consists of a series of indices that are each linked to a basket of 25 CMBS conduit deals issued during a particular year. The indices are used as an indicator of the overall performance of the CRE market and enables investors to make bets on corresponding long and short positions.

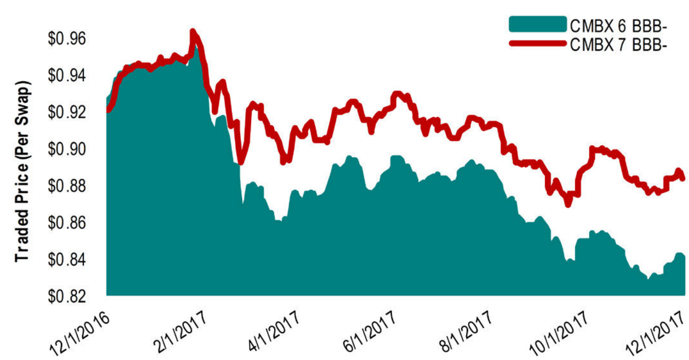
Investors who expect deals in a specific index to get hit with losses can buy protection. That is, they would pay a fixed-rate premium to a seller of protection who would bet against losses. If losses occur, the seller of protection would cover them. So a short trade becomes most profitable when deals in an index suffer actual losses. It also becomes profitable in the event spreads widen, as they have.

The spread blowout in CMBX has been especially pronounced for the 6 and 7 series, which are tied to CMBS issued in 2012 and 2013, largely due to the perceived greater exposure to struggling mall properties and retail bankruptcies. The focus of the trade has been placed on junior bonds lower in the credit stack because the notes are typically the first to incur losses when distressed loans are liquidated or written off.

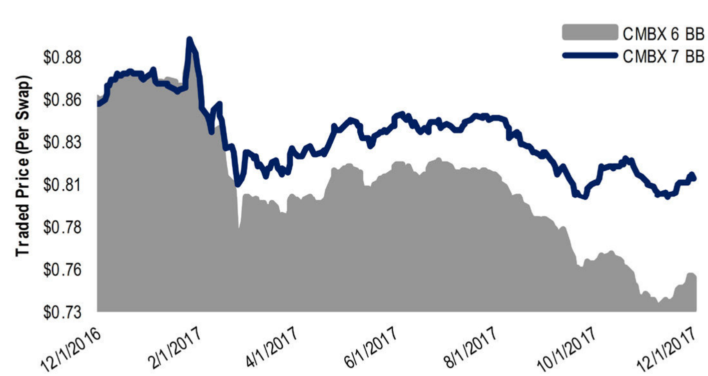
Compared to their tightest levels in late January, BBB- and BB spreads for the two segments initially widened between 130 and 295 basis points, respectively, in just two months as word got out about the trade. While the sell-off took a momentary breather in April, spreads for the BBB- tranches of CMBX 6 and 7 by August had resumed their climb and peaked at a year-to-date high in early November that was 358 and 202 bps wider, respectively, than their lows in January.

By the same token, spreads for the lower credit BB bonds in those same indices reached a high that was a staggering 499 and 254 bps wider than their narrowest point roughly 10 months ago. During this devaluation period, the traded price pegged to the BBB- and BB portions of CMBX 6 and 7 series were reduced by 10 to 17 percent as investors rushed

Traded Price on CMBX 6-7 BBB- Bonds



Traded Price on CMBX 6-7 BB Bonds



Source: Trepp LLC

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to crowd the trade. Prices and spreads for the derivative positions since have recouped some of their losses as the market has begun catching on that the underlying bonds are being priced below their actual worth.

It's no secret that the retail landscape is in the midst of an unprecedented revolution.

The cause of the blowout in CMBX spreads centers on the idea that the weak performance of certain retailers, particularly JCPenney, Sears and Macy's, which often anchor class-B and -C malls, would impact the properties they occupy. The three anchors have been shuttering stores by the dozens.

Such closures often trigger co-tenancy clauses for other in-line mall tenants, prompting them to downsize or vacate altogether. The thinking has been that properties, particularly those in secondary and tertiary markets, exposed to the three would see a greater probability of default and losses. As such, those holding short positions in certain CMBX would see a payout.

But has that bet paid off?

Not quite. Retail loans are the largest exposure for both the CMBX 6 and CMBX 7 indices, with a 38.24 percent and 32.4 percent concentration, respectively. But only 1 percent of the remaining balance of retail assets has been marked as delinquent.

So far, only 40 retail loans in deals tied to the CMBX 6 and 7 series have paid off. And four incurred losses totaling $4.3 million. Each of those was in a deal in the 6 series. No losses have been attributed to deals tied to CMBX 7.

But the number of distressed retail mortgages will likely increase as they inch closer to their scheduled maturity dates and collateral performance continues to deteriorate. ■

CMBX 6 Overview

Property Type	% in CMBX 7	WA LTV %	WA DSCR	WA Debt Yield %	Avg Occupancy %
IN	4.2	64.3	1.8	16.3	95.1
LO	10.7	61.5	2.0	17.5	74.7
MF	5.4	68.4	1.7	12.7	92.9
OF	26.9	66.4	1.7	13.6	90.2
OT	14.6	61.6	2.0	14.1	90.5
RT	38.2	64.2	1.9	15.2	94.4

CMBX 7 Overview

Property Type	% in CMBX 7	WA LTV %	WA DSCR	WA Debt Yield %	Avg Occupancy %
IN	3.9	65.2	1.7	14.6	94.2
LO	13.5	62.7	2.1	17.7	74.0
MF	12.6	73.0	1.6	11.7	92.9
OF	18.3	62.9	1.9	15.4	90.4
OT	19.3	62.3	1.8	14.4	90.5
RT	32.4	62.5	2.1	19.6	95.8

**Based on a December 2017 snapshot*
Source: Trepp LLC

Private-Label CMBS Issuance Surprises With 26.1 Percent Hike in 2017

By Orest Mandzy

The domestic, private-label CMBS market was remarkably healthy last year. A total of 122 deals totaling $86.4 billion priced — up an impressive 26.1 percent from 2016's volumes.

And that's despite the headwind of risk retention. The prevailing wisdom as the year got underway had called for issuance to be no better than flat when compared with 2016. The concern was that the market would be challenged to wrap its arms around the new rules, which require that issuers retain a 5 percent vertical piece of every securitization, or sell a 5 percent subordinate piece by market value to a B-piece buyer. They also can combine the two strategies, keeping a slice and selling off a piece. But the buyers aren't able to hedge, finance or sell their investments for what amounts to a deal's life.

The rules, which went into effect in late 2016, led to a sharp slowdown in issuance early last year. Lenders simply were unsure how to profitably price loans, as it was unclear how buyers of horizontal risk pieces would price those tranches.

Domestic, Private-Label CMBS Issuance

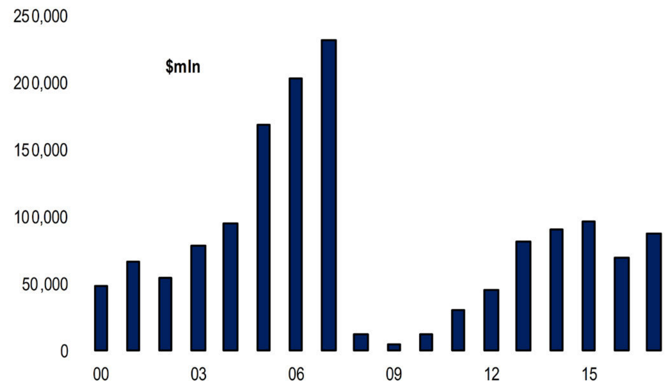
	2017			2016	
Deal Type	# Deals	Vol $mln	Mkt Shr%	# Deals	Vol $mln
Conduit	51	47,443.80	54.90	55	47,078.00
Single-borrower	66	36,401.40	42.10	39	19,445.30
Floating-rate	4	1,578.00	1.80	3	913.50
Non-performing	1	208.50	0.00	0	0.00
Other	1	758.80	0.90	3	1,023.40
Total	**122**	**86,390.40**	**100.00**	**100**	**68,460.20**

Source: Commercial Real Estate Direct

But the period of price discovery was relatively short lived. CD 2017-CD3, a $1.3 billion conduit deal led by Citigroup and Deutsche Bank, was structured with both vertical and horizontal risk-retention pieces, with the latter acquired by KKR & Co., which last year had raised a $1.1 billion fund, KKR Real Estate Credit Opportunity Partners, specifically to make CMBS investments. The deal priced favorably — its benchmark class, with the highest possible ratings and a 10-year average life — printed at a spread of 90 basis points more than swaps. That was some 25 bps inside of a conduit that priced in late December.

Issuers were then off to the races. A survey by the Mortgage Bankers Association found that CMBS lending activity had increased during second quarter by 168 percent from a year earlier and 117 percent from the first quarter.

CMBS Issuance 2017



Source: Commercial Real Estate Direct

The market remained calm all year, with bond spreads — with a small number of exceptions — remaining in a relatively tight band between 76 bps and 98 bps more than swaps. Bond investors lapped deals up, attracted to the relatively generous yields CMBS provided and the asset class' continued healthy credit metrics.

Underwritten debt-service coverage and loan-to-value ratios remained extremely conservative. And the rating agencies weren't arguing much. Moody's Investors Service, for instance, recently said its calculation of LTV had actually declined during the third quarter, while DSCR had increased. Fitch Ratings said much the same, citing the growing presence of loans with investment-grade qualities in conduit pools. But both warned of the growing presence of interest-only loans in collateral pools.

The volume of single-borrower deals skyrocketed in 2017, to 66 deals totaling $36.4 billion from last year's $19.4 billion, while conduit issuance inched up slightly, to $47.4 billion from $47.1 billion.

Further good news: the wall of maturities, which had been a concern for at least the last two years, was cleared without much fuss. But that could have an impact on loan origination volumes going forward. Another potential negative impact is the slowdown in property transactions, a driver of lending activity.

Only $12.1 billion of loans were securitized in 2008, when the MBA said overall lending volumes had declined by 62 percent from the prior year. And through last November, property sales were running 9.1 percent behind 2016, according to Real Capital Analytics. Both data points would indicate weak CMBS lending this year. But some optimists point to the large volumes of short-term loans that were written in recent years, many to recapitalize properties that might have had issues refinancing their CMBS maturities. Nonetheless, few expect CMBS issuance volume to top 2017's level. ■

2H - 2017 Conduit Issuance

Px Date	Trepp Abbr	Amt $mln	AAA JrLvl	BBB-Lvl	Risk Retention Type	Vertical Size %	Horizontal Size (of par) %	Risk Retention Party	UW DSCR	IO %	Px AAA-Sr	PX JRAAA	PX BBB-
14-Jul	BANK 2017-BNK6	933.30	19.00	6.50	Vertical	5.00		WF/BofA/MS	2.80	43.90	92	113	345
21-Jul	JPMCC 2017-JP7	811.00	21.80	7.10	Horizontal		10.30	MassMutual	2.10	50.20	91	115	
24-Jul	CD 2017-CD5	931.70	18.50	6.10	Hybrid	3.80	4.20	Citi/DB/Rialto	2.30	41.70	88	113	375
31-Jul	UBSCM 2017-C2	898.70	18.50	8.90	Horizontal		10.50	KKR	2.30	35.20	90	115	
10-Aug	WFCM 2017-C39	1,132.80	20.60	7.00	Horizontal		10.30	Argentic	2.20	49.40	90	118	
11-Aug	GSMS 2017-GS7	1,081.60	23.10	8.60	Horizontal		10.60	Rialto	2.20	64.70	95	118	325
15-Aug	CGCMT 2017-B1	941.60	20.00	7.00	Vertical	5.00		Citi	2.40	58.80	90	115	360
17-Aug	UBSCM 2017-C3	708.60	19.50	6.50	Horizontal		10.90	KKR	2.20	34.60	94	125	
18-Sep	CGCMT 2017-P8	1,087.10	19.30	6.50	Vertical	5.00		Citi	2.20	43.10	93	125	410
19-Sep	BANK 2017-BNK7	1,213.80	17.50	6.00	Vertical	5.00		WF	2.90	49.30	89	120	370
19-Sep	CSAIL 2017-CX9	858.90	18.10	6.00	Hybrid	2.00	5.70	Natixis/Rialto	3.10	61.40	90	115	375
21-Sep	COMM 2017-COR2	916.50	23.30	8.00	Horizontal		10.50	JeffLoanCore	1.90	42.10	96	125	
29-Sep	UBSCM 2017-C4	818.30	19.50	7.10	Vertical	5.00		Rialto	2.10	37.80	93	120	460
5-Oct	WFCM 2017-C40	705.40	21.60	7.10	Vertical	5.00		WF	2.10	42.40	93	120	450
9-Oct	MSBAM 2017-C34	1,048.60	22.30	7.10	Vertical	5.00		BofA	2.00	42.50	88	120	
13-Oct	JPMDB 2017-C7	1,105.30	20.30	6.50	Hybrid	2.80	6.30	DB/KKR	2.20	49.60	83	113	370
19-Oct	CGCMT 2017-C4	977.10	22.50	8.50	Horizontal		10.50	KKR	1.90	41.90	83	112	
27-Oct	BANK 2017-BNK8	1,130.80	23.90		Vertical	5.00		MS	2.50	65.50	76	100	340
1-Nov	UBSCM 2017-C5	743.40	19.00	6.50	Horizontal		10.50	KKR	2.40	44.80	78	108	
13-Nov	CD 2017-CD6	1,061.90	20.10	7.00	Horizontal		10.00	Argentic	2.20	34.20	75	100	
14-Nov	GSMS 2017-GS8	1,020.40	23.10	7.80	Horizontal		10.40	KKR	2.30	52.20	77	105	
17-Nov	WFCM 2017-C41	785.90	21.10	7.60	Horizontal		10.50	Argentic	1.90	32.60	79	110	
17-Nov	CSAIL 2017-CX10	855.30	19.10	5.80	Hybrid	4.10	0.90	Natixis/ Eightfold	2.70	68.10	77	98	375
21-Nov	CCUBS 2017-C1	696.80	21.80	7.40	Horizontal		10.50	KKR	2.10	71.50	84	120	
1-Dec	UBSCM 2017-C6	684.70	18.90	6.10	Vertical	5.00		Rialto	2.20	40.60	83	118	425
5-Dec	BANK 2017-BNK9	1,053.70	23.90	6.90	Vertical	5.00		MS/BofA/WF	2.40	57.20	81	110	350
12-Dec	WFCM 2017-C42	744.80	24.30	7.80	Vertical	5.00		WF	2.00	44.90	84	110	410
12-Dec	MSC 2017-HR2	942.70	23.80	7.80	Horizontal		10.20	Argentic	2.30	67.20	83	113	
20-Dec	UBSCM 2017-C7	891.00	18.90	4.10	Horizontal		10.90	Prime Finance	2.10	33.90	87	125	

Source: Commercial Real Estate Direct

From the Agora to the Forum to the Shopping Mall

By Jen Loukedis

A Greek agora.
Source: Wikipedia.com

The ancient Greeks had the agora and the Romans had their forums, but the indoor shopping mall is purely a modern creation.

While shopping centers and retailing districts had existed in the United States for decades, the totally enclosed mall was the post-war vision of a European socialist. An enclosed, climate-controlled retailing mecca, the mall was envisioned to be more than just a place to buy goods. It also would be a place to gather and socialize. While today the mall is ubiquitous, it is hard to believe it once was considered revolutionary.

Malls were part of the post-war expansion and had their heyday during the Reagan years. Here's a look back at the events that got the mall to where it is today.

1945 World War II ends and millions of American soldiers, sailors and Marines return home. As a result of the Servicemen's Readjustment Act of 1944, commonly referred to as the G.I. Bill of Rights, veterans were able to obtain low-interest, zero down-payment home loans. Favorable terms were provided for newly constructed homes, which encouraged families to move out of urban apartments and into suburban homes.

One of the first American suburbs.
Source: History.com

1951 Austrian-born Victor Gruen forms an architectural firm, where he envisions a "third place" for suburbanites — an environment filled with retail, greenery and light that could serve to get people out of their cars and connect socially.

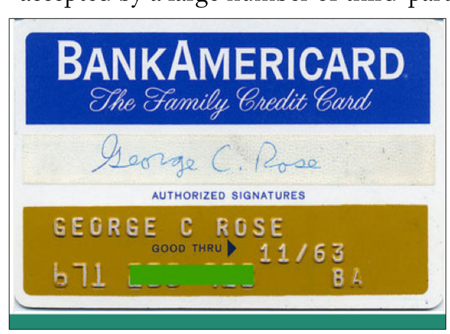
His original vision resembled the mixed-use developments of today, with a core of retail surrounded by residential, office and school space.

Source: Victor Gruen Collection, American Heritage Center, University of Wyoming.

1956 Southdale Mall opens in Edina, Minn., about 10 miles southwest of Minneapolis. The two-level enclosed property, which cost $20 million, included two department store anchors, 72 specialty stores and parking for 5,000 cars. A light-filled interior, the "Garden Court of Perpetual Spring," included a goldfish pond, sculpture and sidewalk café. Southdale Mall is considered the first enclosed mall in the U.S. and became a template for many others that followed.

Southdale Mall
Source: Wikimedia Commons

1958 Bank of America introduces the BankAmericard, the first credit card to be accepted by a large number of third-party sellers.



1962 Bank of America Credit Card
Source: CreditCardCompare.Com.au

1960 The REIT Act is signed into law, allowing investors to band together to invest in large-scale, diversified portfolios of income-producing real estate.
Today, publicly-traded mall REITs control about 80 percent of the U.S. malls by asset value, according to Green Street Advisors.

1962 Walmart, Kmart and Target open their doors, relying on low costs and high turnover to provide customers with lower prices.

Source: Flickr

1966 "Black Friday" enters the retail lexicon.

1970 Some 300 enclosed shopping malls populate the country, according to the International Council of Shopping Centers.

1974 The first product bearing a bar code, a pack of gum, is scanned at a supermarket in Troy, Ohio.

1989 British scientist Tim Berners-Lee, who is often referred to simply as TimBL, develops what we now know as the World Wide Web.

1992 Mall of America, then the country's largest mall at 4.2 million square feet, opens in Bloomington, Minn.

Source: Flickr

1993 Sears eliminates its general merchandise catalog.

Source: Pintrest

1995 Amazon.com sells its first book.

2001 Apple Inc. opens its first store, in Tysons Corner, Va.

2005 Federated Department Stores agrees to buy The May Department Stores Co. for $11 billion in stock. The new company is renamed Macy's. Meanwhile, Cyber Monday first appears in a press release to describe the Monday after Thanksgiving, when American consumers returned to work and shopped online.

2011 The national vacancy rate for malls in America is 9.4 percent, according to Reis Inc.

2017 The number of malls in the country declines to about 1,100, from 1,500 in 2002, according to the ICSC. Credit Suisse predicts up to 25 percent, or 275, of these malls will close by 2021. The national vacancy rate for malls in the U.S. stands at 8.3 percent, according to Reis.

CMBS Defeasance Activity Nose Dives As Maturity Wall Is Hurdled

By Orest Mandzy

The dwindling size of the legacy CMBS market has had a profound impact on defeasance activity.

Only 413 CMBS loans with a balance of $5.9 billion were defeased, or replaced by government securities, last year through the end of November. That compares with the 1,013 loans totaling $15.4 billion that were defeased during the same period a year earlier.

While market conditions last year were prime for defeasance transactions, there just weren't that many loans to defease.

Defeasance activity flourishes when interest rates are low and property values are high, as was the case last year. It's further bolstered when the difference between short- and long-term interest rates narrows — when the yield curve flattens. That, too, took place.

The big wave of defeasance occurred between 2013 and 2016, when some $70.6 billion of loans were replaced by government securities. That coincided with the CMBS wall of maturities.

"We're nearing the 10-year mark from the financial crisis," explained Dan Kahler, director of defeasance at Chatham Financial, a Kennett Square, Pa., advisory firm with a substantial defeasance business. "After the crisis, not a lot of CMBS was issued. With fewer maturities, we're seeing fewer defeasances in the pipeline."

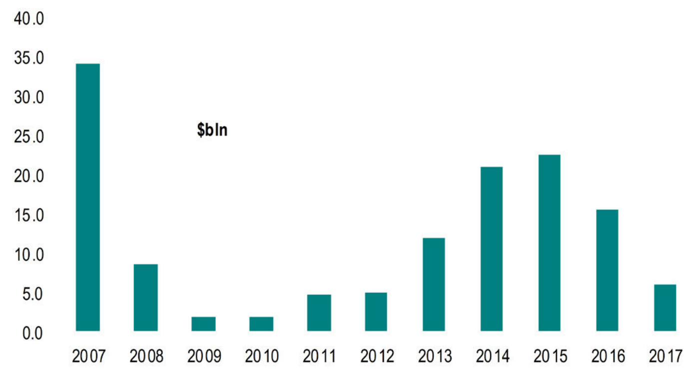
Now that maturity volumes are declining, so are defeasance volumes. The expectation is that volume will remain steady, but muted. After all, only $12.1 billion of loans were securitized in 2008, $3.6 billion in 2009 and $11 billion in 2010.

The big variable, according to Eitan Weinstock of AST Defeasance Services of Los Angeles, is the expectation of dramatic interest-rate hikes. That, he explained, would move borrowers to lock in current rates and defease existing loans. But the rate moves have to be dramatic. "Libor moved up one percentage point," he explained. "And it wasn't enough to scare people" into completing transactions. "It has to be a real number … then, even if they have six years left on their loans, they'll say, 'let's do it.'"

Commercial mortgages, particularly those that are securitized, typically are structured with prepayment restrictions to ensure that lenders receive the cash flows they expect for the life of their loans. Borrowers who decide to pay off their loans before they become open to prepayment — say in the event of a sale or if interest rates drop sharply — would face penalties that could be onerous. But they could replace their mortgage collateral with government securities that would mimic the cash flow of the mortgage.

So, the cost to defease a mortgage increases as its remaining term increases. As a result, most defeasance activity takes place within two years of a loan's maturity.

Defeasance Volume



Source: Commercial Real Estate Direct

If a property's value climbs, as generally has been the case, given that the Real Capital Analytics Commercial Property Price Index is now 21.1 percent higher 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.

However, 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, Chatham Financial, Bank of America, Wells Fargo Bank, Trimont Real Estate Advisors of Atlanta and Commercial Defeasance and Waterstone Capital Advisors, both of Charlotte, N.C.

Just how costly a defeasance transaction can be was exemplified by the refinancing of $875 million of debt against Manhattan's Worldwide Plaza. The 2.1 million-square-foot office property was recapitalized late last year when RXR Realty and SL Green Realty Corp. bought a 48.7 percent stake in it from New York REIT Inc.

The property, at 825 Eighth Ave., early last year was appraised at a value of $1.74 billion, nearly 30 percent more than the $1.35 billion value pegged to it in 2013 when it last was financed.

As a result, it was able to support a much larger financing package. Goldman Sachs had provided $1.2 billion of interest-only debt, including $260 million of mezzanine financing, all with a blended coupon of 3.98 percent. That was used to defease the existing debt, a $710 million senior piece that was securitized through COMM, 2013-WWP. The debt, with a 4.52 percent blended coupon, required only interest payments for the first five years, then amortizes on a 35-year schedule.

The cost to defease the old financing: $109 million. ■

Top Defeased Loans - 2017

Mo. of Defeasance	Trepp ID	Property Name	Location	Property Type	Balance $mln	Coupon %	DSCR	NOI $mln	Maturity Date
November	COMM 2013-WWP	Worldwide Plaza	Manhattan	OF	710.00	4.00	1.87	73.90	March 10, 2023
February	JPMCC 2009-IWST	IWEST Portfolio	Various	RT	379.03	7.50	2.02	61.11	Dec. 1, 2019
February	COMM 2007-C9	60 Wall Street	Manhattan	OF	285.00	5.77	1.33	71.74	July 1, 2017
	CSMC 2007-C5	60 Wall Street	Manhattan	OF	130.00				
	MSC 2007-IQ16	60 Wall Street	Manhattan	OF	125.00				
September	JPMCC 2005-CB11	Airport Industrial Park	Honolulu	IN	90.46	5.56	1.94	11.04	Jan. 1, 2020
March	MSBAM 2012-C6	Hyatt Regency Austin	Austin, Texas	LO	71.91	5.00	2.07	10.13	Aug. 10, 2017
October	UBSBB 2013-C5	231 South LaSalle	Chicago	OF	68.49	4.16	1.99	4.80	Dec. 6, 2022
November	JPMCC 2011-C4	Sheraton Chicago Hotel & Towers - Fee Interest	Chicago	OT	68.00	5.52	1.15	5.54	March 1, 2018
May	COMM 2014-CR18	Mellon Independence Center	Philadelphia	MU	64.49	4.51	1.54	6.13	May 5, 2019
February	MSC 2008-T29	Cabin John Mall & Shopping Center	Potomac, Md.	RT	63.92	6.53	1.32	5.86	Jan. 1, 2018
January	COMM 2013-CR13	iStorage Portfolio 3	Various	SS	50.98	5.03	1.38	4.61	Dec. 6, 2023
September	GSMS 2013-GC14	Mendoza Multifamily Portfolio	Various	MF	48.03	4.83	2.46	4.61	June 6, 2023
January	MLCFC 2007-9	Cayre Portfolio	Various	MU	45.20	7.04	0.75	4.76	Oct. 5, 2017
March	CGCMT 2013-GC11	Radisson Bloomington	Bloomington, MInn.	LO	42.01	4.49	2.24	6.42	March 6, 2018
January	COMM 2007-C9	Congressional Village	Rockville, Md.	RT	41.53	6.36	1.06	3.52	July 1, 2017
January	CWCI 2007-C3	Walgreens Portfolio	Various	RT	40.00	5.61	1.26	2.91	May 11, 2017
November	MSBAM 2013-C10	Boston Hospitality Portfolio	Various	LO	39.22	4.23	2.03	8.83	May 1, 2023
August	WFRBS 2012-C9	Grand Cayman Marriott Beach Resort	Cayman Islands	LO	37.65	5.05	2.32	6.87	Nov. 1, 2022
January	JPMCC 2012-CBX	Centre Market Building	Newark, N.J.	OF	36.30	6.18	1.68	8.61	April 1, 2018
June	COMM 2014-CR17	Indigo on Forest	Dallas	MF	33.46	4.73	1.73	6.00	May 6, 2024
January	CGCMT 2013-GC11	Westin Memphis	Memphis, Tenn.	LO	32.64	5.00	2.49	4.09	April 6, 2018
January	JPMCC 2007-CB19	Crossroads Center	Bartonsville, Pa.	RT	31.00	5.77	1.35	2.34	June 1, 2017
September	MLMT 2007-C1	U-Haul SAC 14	Various	SS	30.69	6.13	1.34	3.62	July 8, 2037
January	MSC 2007-IQ16	Centerpoint Medical Office Building	Independence, Mo.	OF	30.39	5.69	1.35	2.62	July 1, 2017
January	JPMCC 2006-CB15	Kaiser Foundation Building	Redwood City, Calif.	OF	30.05	6.07	1.40	3.16	July 1, 2018
August	GSMS 2013-GC16	Walnut Creek Marriott	Walnut Creek, Calif.	LO	29.81	5.04	2.11	3.62	Sept. 6, 2018
July	JPMBB 2014-C25	Florida Multifamily Portfolio	Various	MF	29.75	4.65	2.07	7.34	Nov. 1, 2024
September	MLMT 2007-C1	U-Haul SAC 17	Various	SS	29.13	6.13	1.33	3.55	July 8, 2037
June	MSC 2008-T29	Arena Hub Shopping Center	Wilkes-Barre, Pa.	RT	29.09	6.25	1.38	3.67	Jan. 1, 2018
September	MLMT 2007-C1	U-Haul SAC 15	Various	SS	28.42	6.13	1.55	3.43	July 8, 2037
June	WFRBS 2014-LC14	Marriott Courtyard - Maui	Kahului, Hawaii	LO	27.17	5.13	1.74	3.25	Feb. 1, 2024
February	JPMCC 2012-CBX	Slate Portfolio	Various	RT	26.63	5.80	1.79	3.64	April 30, 2021
November	WFRBS 2011-C4	Bayshore Club Apartments and Summerhill Villas Apartments	Las Vegas	MF	25.76	6.06	1.34	2.74	May 1, 2021
October	CSFB 2005-C5	Kings Village Corp.	Brooklyn, N.Y.	CH	25.63	5.55	0.73	6.49	July 1, 2020
September	DBUBS 2011-LC3A	Creekside at Taylor Square	Reynoldsburg, Ohio	MF	25.32	5.54	1.41	2.69	May 6, 2021
March	CSMC 2007-C5	Ivy Club Apartments	Landover, Md.	MF	25.07	5.65	1.17	2.10	Oct. 11, 2017
July	GCCFC 2007-GG11	955 Massachusetts Avenue	Cambridge, Mass.	OF	24.62	6.70	1.17	2.36	Oct. 6, 2017
April	GSMS 2013-GC12	Commerce Park	Danbury, Conn.	IN	24.28	4.90	1.66	2.74	Jan. 6, 2023
March	GSMS 2011-GC5	250 Mercer Street	Manhattan	RT	23.80	5.31	1.39	2.35	July 6, 2021

Source: Commercial Real Estate Direct

2017 CMBS Award Winners

Goldman Sachs Takes Top Honors Among CMBS Bookrunners, Lenders

By Orest Mandzy

Goldman Sachs last year contributed an industry-leading $11.7 billion of commercial mortgages to CMBS deals, which was instrumental in it taking the top spot among CMBS bookrunners.

The investment bank handled bookrunner duties on 18.1 transactions totaling $11.8 billion, or 13.7 percent of the year's $86.4 billion of issuance. That was up substantially from 2016, when it participated as bookrunner on 11.1 percent of that year's issuance volume.

JPMorgan Securities was well behind it in both the ranking of bookrunners and loan contributors. It had contributed $10.1 billion of loans to the market and received bookrunner credit for 14.5 deals totaling $11 billion, or 12.7 percent of issuance.

The bookrunner ranking counts only private-label CMBS deals. That is, transactions backed solely by non-agency mortgages. It divvies up credit proportionally among all of a deal's bookrunners, based on information gleaned from offering materials.

Goldman was the sole loan contributor and bookrunner on four conduit deals that totaled $4.1 billion. It also contributed $7.6 billion of loans to a total of 22 single-borrower transactions. In eight of those deals, it was the sole loan contributor and bookrunner.

Among the big-ticket deals it participated in was Cold Storage Trust, 2017-ICE3, a $1.3 billion deal, in which JPMorgan also participated, that allowed Lineage Logistics to refinance debt against a portfolio of 54 cold-storage properties. It also contributed the lion's share of a $705 million loan against Manhattan's Worldwide Plaza office property. That loan was securitized through Worldwide Plaza Trust, 2017-WWP.

Its dominant participation in the large-loan business skewed the average size — $79.8 million — of the loans it contributed to the CMBS market. Only Credit Suisse and JPMorgan had a larger average loan size — $108.1 million and $86 million, respectively.

On the other end of that spectrum were C-III Commercial Mortgage, with an average loan size of $4.9 million, and

Continued on next page

Top Managers of Domestic, Private-Label CMBS

	2017			2016		
Investment Bank	#Deals	Bal $mln	Mkt Shr%	#Deals	Bal $mln	Mkt Shr%
Academy Securities	34	30,876.20	35.70	39	30,982.70	45.30
Citigroup	34	29,346.20	34.00	26	20,525.90	30.00
Deutsche Bank	33	26,822.90	31.00	27	19,714.00	28.80
Morgan Stanley	27	23,267.60	26.90	17	13,057.70	19.10
JPMorgan Securities	27	23,045.00	26.70	22	15,120.20	22.10
Drexel Hamilton	22	21,929.60	25.40	31	25,009.10	36.60
Wells Fargo Securities	26	19,798.10	22.90	20	13,654.40	20.00
Goldman Sachs	26	18,563.90	21.50	19	14,388.10	21.10
Barclays Capital	19	16,441.30	19.00	14	9,799.00	14.30
BofA Merrill Lynch	18	15,752.10	18.20	14	9,634.90	14.10
Natixis	16	11,442.10	13.20	9	6,186.70	9.10
UBS Securities	14	10,495.50	12.10	9	7,080.00	10.40
Credit Suisse	13	5,858.00	6.80	6	3,539.20	5.20
Cantor Fitzgerald	6	4,637.50	5.40	9	6,820.00	10.00
KeyBank	5	4,035.50	4.70	7	5,307.60	7.80
CIBC World Markets	3	2,676.00	3.10	3	2,747.80	4.00
Jefferies	1	916.50	1.10	4	3,660.10	5.40
CastleOak	1	644.70	0.70	5	4,010.80	5.90

Full Credit to Every Manager on a Deal
Source: Commercial Real Estate Direct

Top Bookrunners Domestic, Private-Label CMBS

	2017			2016		
Investment Bank	#Deals	Bal $mln	Mkt Shr%	#Deals	Bal $mln	Mkt Shr%
Goldman Sachs	18.09	11,819.34	13.68	10.05	7,563.72	11.07
JPMorgan	14.52	10,968.11	12.70	14.94	10,350.16	15.14
Citigroup	12.04	10,012.71	11.59	10.87	8,061.79	11.80
Wells Fargo	14.27	9,936.06	11.50	13.36	9,513.96	13.92
Deutsche Bank	12.80	9,879.74	11.44	14.21	9,926.60	14.52
Morgan Stanley	12.86	9,536.77	11.04	7.36	5,091.85	7.45
Bank of America	8.75	5,910.78	6.84	7.24	4,257.04	6.23
Barclays Capital	6.66	5,269.62	6.10	4.69	3,096.56	4.53
UBS	5.67	4,203.40	4.87	3.19	2,432.68	3.56
Credit Suisse	9.21	3,807.42	4.41	5.29	3,224.51	4.72
Natixis	3.94	1,960.81	2.27	0.50	125.80	0.18
Cantor Fitzgerald	1.91	1,324.29	1.53	4.41	3,019.53	4.42
Societe Generale	1.77	1,274.72	1.48	2.79	1,622.18	2.37
Jefferies	0.53	486.65	0.56	0.00	0.00	0.00
CIBC	0.00	0.00	0.00	0.00	0.00	0.00
Scotia Bank	0.00	0.00	0.00	0.00	0.00	0.00
KeyCorp	0.00	0.00	0.00	0.10	55.70	0.08
Total	122.00	86,390.43	100.00	99.00	68,342.07	

Source: Commercial Real Estate Direct

2017 CMBS Award Winners

Continued from previous page

NCB FSB, with an average loan size of $3.3 million.

In total, 29 lenders contributed loans to CMBS deals last year. That was down from 38 in 2016. Among those that quit the CMBS market last year were Walker & Dunlop, which found that its clients weren't clamoring for conduit loans. It also was prompted by the increased capital that would be needed to play a role in the sector, post risk retention.

The reduction in the number of active lenders in the market was expected, as several smaller players quit in late 2016 because of their inability to consistently profit from originating loans for securitization. The risk-retention rules contributed to some exits.

Others that didn't contribute loans in 2017, but did the year before included Prudential Financial, whose Liberty Island Group conduit-lending venture, with Perella Weinberg Partners' Asset Based Value Strategy, was dissolved in mid-2016.

Meanwhile, a ranking that gives full credit to every manager on a deal had Academy Securities at the top, with 34 deals totaling $30.9 billion, or 35.7 percent of the year's issuance. That compares with 39 deals in 2016, when its market share was a whopping 45.3 percent. It took top honors that year, as well.

Academy is a disabled veteran-owned institution that 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 best known for his years as a wide receiver for the New York Giants professional football team. He played on the team when it won the Super Bowl in 1986.

JPMorgan 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.

Citigroup was just behind Academy in that ranking, managing 34 deals totaling $29.3 billion, or 34 percent of the year's volume. It was followed by Deutsche Bank, with 33 deals totaling $26.8 billion, or a 31 percent share. ■

Top Loan Contributors

2017				2016	
Loan Contributors	#loans	Vol $mln	Mkt Shr%	Vol $mln	Mkt Shr%
Goldman Sachs	146.90	11,719.30	13.60	7,288.40	11.20
JPMorgan Chase Bank	117.70	10,114.10	11.80	8,965.80	13.70
Deutsche Bank	198.50	9,690.00	11.30	6,604.10	10.10
Morgan Stanley	166.20	8,539.80	9.90	4,083.90	6.30
Citigroup	199.10	8,088.20	9.40	5,512.20	8.40
Wells Fargo Bank	260.10	6,071.50	7.10	3,572.30	5.50
Bank of America	161.00	5,165.50	6.00	3,240.30	5.00
Barclays Bank	124.70	4,917.40	5.70	2,959.80	4.50
Credit Suisse	28.50	3,079.80	3.60	1,530.20	2.30
Natixis	96.10	2,507.90	2.90	1,895.30	2.90
UBS Real Estate Securities	148.40	2,497.40	2.90	2,432.00	3.70
Rialto Mortgage Finance	138.00	1,658.70	1.90	1,932.20	3.00
Starwood Mortgage Finance	117.70	1,534.10	1.80	1,739.00	2.70
Ladder Capital Finance	114.00	1,476.10	1.70	1,349.50	2.10
Cantor Commercial	81.00	1,326.20	1.50	3,212.50	4.90
Societe Generale	55.50	1,269.70	1.50	1,083.80	1.70
Argentic Real Estate Finance	86.50	1,263.60	1.50	771.40	1.20
KeyBank	58.00	921.70	1.10	758.10	1.20
Benefit Street Partners	52.00	777.00	0.90	1,241.20	1.90
Lonestar/Relius	30.00	758.80	0.90	506.30	0.80
Jefferies LoanCore	23.00	486.80	0.60	1,110.20	1.70
Principal Commercial	20.00	460.60	0.50	478.70	0.70
RAIT RBS	23.00	342.40	0.40	21.40	0.00
CIBC World Markets	27.00	318.10	0.40	273.70	0.40
Bancorp Bank	15.00	314.40	0.40	367.00	0.60
NCB FSB	88.00	288.40	0.30	444.80	0.70
C-III Commercial Mortgage	44.00	217.00	0.30	367.70	0.60
Blackstone Mortgage Trust	0.20	100.00	0.10	0.00	0.00
Basis Real Estate Capital	9.00	74.30	0.10	156.00	0.20
Bank of New York	0.00	0.00	0.00	488.40	0.70
A10 Capital	0.00	0.00	0.00	251.60	0.40
MC-Five Mile	0.00	0.00	0.00	182.70	0.30
Bank of China	0.00	0.00	0.00	110.00	0.20
KGS-Alpha Real Estate	0.00	0.00	0.00	74.70	0.10
Redwood Mortgage Trust	0.00	0.00	0.00	72.20	0.10
Liberty Island Group	0.00	0.00	0.00	67.90	0.10
Prudential Financial	0.00	0.00	0.00	65.00	0.10
Walker & Dunlop	0.00	0.00	0.00	55.90	0.10
Freedom Commercial	0.00	0.00	0.00	9.50	0.00

Source: Commercial Real Estate Direct

2017 CMBS Award Winners

Rialto Keeps B-Piece Crown; KKR Tops Risk-Retention Ranking

By Orest Mandzy

Rialto Capital Management maintained its position as the most-active buyer of B-pieces from CMBS conduit transactions last year. It bought into 14 deals totaling $12.9 billion, or 27.2 percent of the year's issuance.

But only six of its investments were subject to the risk-retention rules that went into effect in late 2016. The rest of the deals it bought into had vertical risk-retention structures, where issuers retained 5 percent slices of each.

KKR Real Estate Credit Opportunity Partners was just behind Rialto in the B-piece ranking, buying into 12 deals totaling $10.9 billion, or 23 percent of the year's conduit issuance.

But all its investments contributed to meeting the deals' risk-retention requirements. So, it topped a ranking of B-piece buyers whose investments were subject to risk-retention rules.

The rules, which were implemented with the idea that if issuers kept some of what they originate, they'd remain disciplined, require that issuers keep a 5 percent slice — by face value — of their deals. However, they could sell off 5 percent of a deal's subordinate bonds — by market value. They also could blend both approaches, keeping a piece and selling another.

The buyer of a horizontal slice is restricted from leveraging, hedging or selling their investment for at least five years.

That makes the risk-retention ranking more significant. KKR effectively must retain, for at least five years, and likely for the deals' duration, the $947.1 million of bonds it bought. Last year, it had raised $1.1 billion of equity commitments for a fund, giving it the type of long-term capital needed for its investments. Those were priced to yield from 14.15 percent to 18.25 percent, depending on how high up a deal's capital stack it went.

Six of the deals the company invested in were structured with horizontal risk-retention slices, where KKR would buy roughly 10.5 percent, by par value, of deals' most subordinate bonds. The other six had hybrid structures, where both a horizontal and vertical slice were carved out to meet the risk-retention requirement. In those cases, KKR would buy 6.3 percent to 8.3 percent of a deal's most junior bonds, while its issuer would retain a vertical slice equal to 1.9 percent to 2.8 percent.

Top Buyers of CMBS Conduit B-Pieces

	2017			2016		
Bpce Buyer	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
Rialto Capital Advisors	14.00	12,925.70	27.20	16.00	13,477.70	28.60
KKR Real Estate Credit	12.00	10,897.50	23.00	1.00	1,026.80	2.20
Argentic Real Estate	6.00	5,648.20	11.90	0.00	0.00	0.00
Prime Finance	5.00	4,810.80	10.10	3.10	2,614.30	5.60
Eightfold Real Estate	4.70	4,640.50	9.80	9.00	7,911.60	16.80
LNR Securities	2.40	2,471.20	5.20	3.30	2,946.90	6.30
MassMutual	2.00	1,854.50	3.90	0.00	0.00	0.00
BlackRock Realty	1.00	977.10	2.10	3.00	2,910.90	6.20
NorthStar Real Estate	1.00	959.00	2.00	0.00	0.00	0.00
Jefferies LoanCore	1.00	916.50	1.90	1.00	890.70	1.90
Resource Capital Corp.	1.00	705.40	1.50	0.00	0.00	0.00
C-III Capital Partners	1.00	637.60	1.30	4.00	3,148.60	6.70
Torchlight	0.00	0.00	0.00	4.00	3,342.40	7.10
Ellington	0.00	0.00	0.00	3.60	2,682.30	5.70
Och Ziff	0.00	0.00	0.00	2.00	1,867.40	4.00
Seer	0.00	0.00	0.00	2.00	1,509.80	3.20
Basis	0.00	0.00	0.00	1.00	1,022.90	2.20
World Class	0.00	0.00	0.00	1.00	955.00	2.00
Raith	0.00	0.00	0.00	1.00	771.00	1.60
Total	**51.00**	**47,443.80**		**55.00**	**47,078.00**	

Buyers of CMBS Conduit Horizontal Risk-Retention Pieces

Investor	# Deals	Face Amt of Bonds Bought $Mln	Mkt Shr%
KKR Real Estate Credit	12	947.10	36.10
Argentic Real Estate Finance	5	515.20	19.70
Rialto Capital Advisors	6	429.00	16.40
MassMutual	2	188.80	7.20
Prime Finance	2	169.80	6.50
LNR Securities	1	112.00	4.30
NorthStar Real Estate Income Trust	1	102.60	3.90
Jefferies LoanCore	1	96.20	3.70
Eightfold Real Estate Capital	2	59.90	2.30
Total	**32**	**2,620.70**	**100.00**

Source: Commercial Real Estate Direct

Well behind KKR in the conduit risk-retention ranking was Argentic Real Estate Finance, which invested in five deals totaling $515.2 million. All of its deals had horizontal risk-retention structures. ■

2017 CMBS Award Winners

Special Servicer Ranking - 2017

	2017									2016		
	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%
Midland Loan Services	21	18,090.20	20.90	17	15,666.20	33.00	3	2,021.80	5.60	15	12,139.80	17.8
Rialto Capital Advisors	14	12,925.70	15.00	14	12,925.70	27.20			0.00	16	13,477.70	19.7
KeyBank	15	11,677.30	13.50	3	3,132.70	6.60	11	8,025.50	22.00	9	5,158.20	7.5
LNR Partners	11	10,431.20	12.10	10	9,476.20	0.20	1	955.00	2.60	7	5,948.50	8.7
Aegon USA Realty Advisors	23	9,793.60	11.30				23	9,793.60	26.90	13	6,349.80	9.3
Wells Fargo Bank	17	9,635.50	11.20			0.00	17	9,635.50	26.50	12	6,926.30	10.1
CWCapital Asset Management	5	4,900.00	5.70	5	4,900.00	10.30			0.00	9	7,265.70	10.6
Trimont Real Estate	6	4,107.90	4.80			0.00	4	3,585.00	9.80	3	1,474.50	2.2
Cohen Financial	5	1,580.00	1.80			0.00	5	1,580.00	4.30			
C-III Asset Management	2	1,342.90	1.60	2	1,342.90	2.80			0.00	5	3,919.50	5.7
Strategic Asset Services	1	805.00	0.90			0.00	1	805.00	2.20	1	264.00	0.4
Hudson Advisors	1	758.80	0.90			0.00			0.00	1	506.30	0.7
RAIT Financial Trust	1	342.40	0.00			0.00			0.00			
Torchlight Loan Services										5	3,504.40	5.1
Talmage LLC										2	1,155.00	1.7
Total	**122**	**86,390.40**		**51**	**47,443.80**		**65**	**36,401.40**		**98**	**68,089.70**	

Source: Commercial Real Estate Direct

Master Servicer Ranking - 2017

	2017									2016		
	Total			Conduit			Single-borrower			2016		
	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
Wells Fargo Bank	76	54,478.90	63.10	34	31,332.40	66.00	40	21,671.20	59.50	61	44,196.40	64.70
Midland Loan Services	18	15,989.00	18.50	15	14,397.20	30.30	3	1,591.80	4.40	16	11,711.10	17.10
KeyBank	26	15,371.70	17.80	2	1,714.20	3.60	23	13,138.40	36.10	21	12,182.20	17.80
RAIT Financial Trust	1	342.40	0.40			0.00			0.00			
Trimont Real Estate Advisors	1	208.50	0.20			0.00			0.00			
Total	**122**	**86,390.40**	**100.00**	**51**	**47,443.80**	**100.00**	**66**	**36,401.40**	**100.00**	**98**	**68,089.70**	

Source: Commercial Real Estate Direct

2017 CMBS Award Winners

Fitch Tops Moody's in CMBS Rating Agency Ranking

By Orest Mandzy

Newsflash: Moody's Investors Service was not last year's most-active rating agency in the CMBS sector.

While it rated an enviable 62.6 percent of all transactions, it was topped by Fitch Ratings, which rated two of every three deals issued last year, including all 51 conduit transactions.

Moody's, meanwhile, wasn't tapped to rate five of 2017's conduit deals. That's in contrast to the previous year, when it rated every one of the 55 conduit deals that were issued. And like during 2016, it hasn't been hired to rate all bonds in a transaction. Typically, issuers will use only its ratings up to a deal's junior-AAA class. And Moody's ratings are typically two notches lower than its competitors for those classes.

Another surprise in the CMBS universe last year was the come-back by Standard & Poor's. The company rated 59 of the year's 122 deals, including 10 conduits, for a 42.3 percent share of the market. It dominated the single-borrower market, with a sector-leading 72.7 percent market share.

S&P's overall market share last year was up from a 22 percent share a year earlier, when the rating agency's one-year disbarment from the conduit sector was lifted. That year, it had rated only three conduit deals.

Many investors, predominantly money managers and mutual funds, require the fixed-income securities they buy to have ratings from at least one of what many call the "major" rating agencies — Moody's, Fitch and S&P. That generally has worked to the detriment of the remaining three agencies, DBRS, Kroll Bond Rating Agency and Morningstar Credit Ratings. After all, issuers have used Moody's ratings only for deals' most senior classes. But every conduit deal issued last year had three rating agencies, and eight deals had four.

DBRS benefited most. Its market share increased sharply, to 30.4 percent from 25.4 percent, while Kroll's improved slightly. ■

Domestic Private-Label CMBS Rankings - Rating Agencies

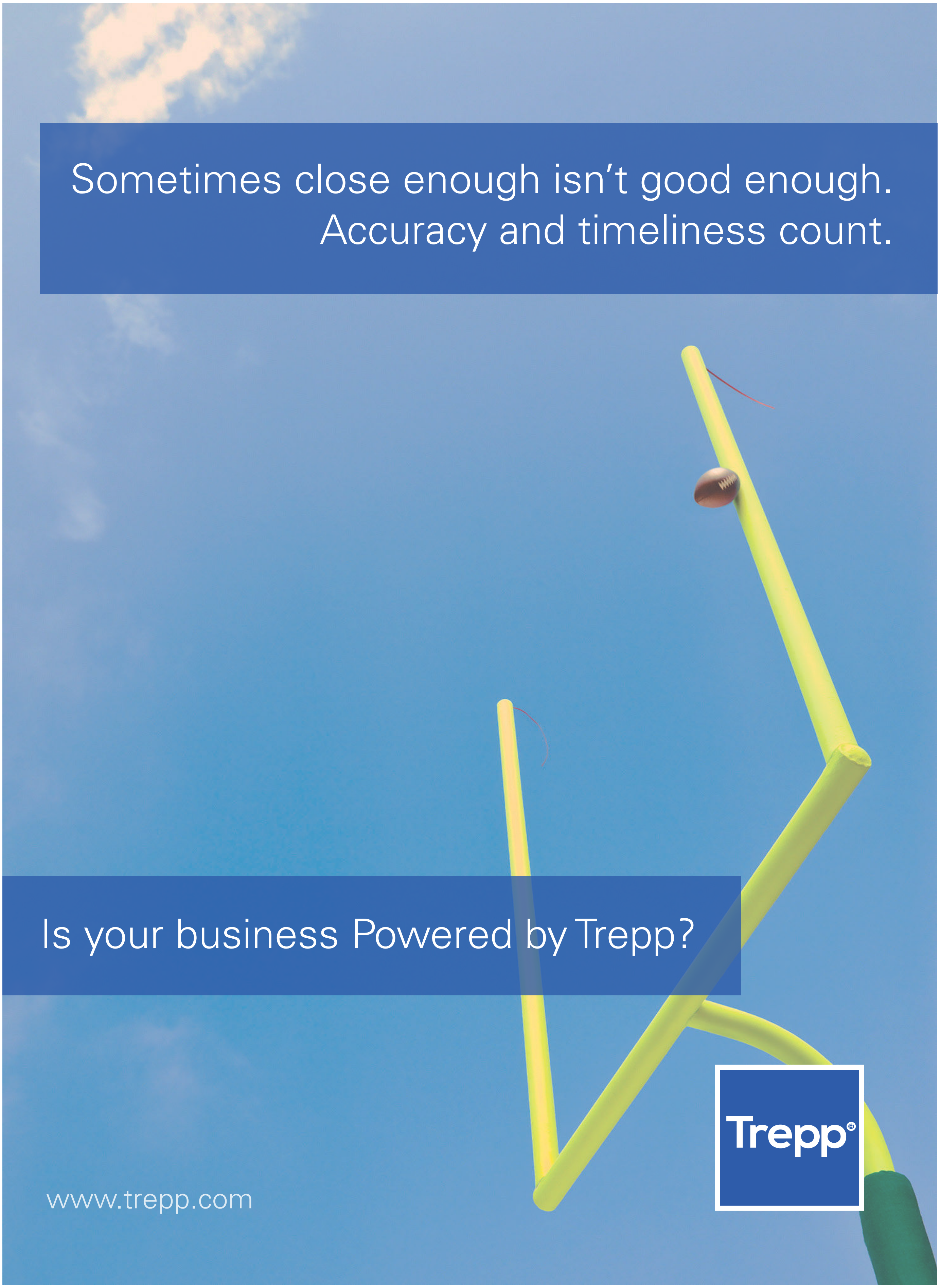
	Total			Conduit			Single-Borrower			2016		
Rating Agencies	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
Fitch	66	57,682.30	66.80	51	47,443.80	100.00	14	9,479.70	26.00	62	50,786.60	74.30
Moody's	62	54,090.30	62.60	47	43,864.70	92.50	12	8,810.10	24.20	72	57,065.30	83.50
Kroll	54	45,397.50	52.50	41	28,377.60	59.80	19	15,395.90	42.30	45	34,894.80	51.10
S&P	59	36,543.40	42.30	10	9,162.80	19.30	47	26,459.40	72.70	32	14,889.80	21.80
DBRS	35	26,299.70	30.40	19	17,856.30	37.60	15	7,924.30	21.80	25	17,353.70	25.40
Morningstar	22	11,138.50	12.90	2	2,020.90	4.30	19	8,715.40	23.90	22	13,687.40	20.00

Source: Commercial Real Estate Direct

Trustee Ranking

	Total			Conduit			Single-Borrower			2016		
Trustees	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%	#Deals	Vol $mln	Mkt Shr%
Wilmington Trust	75	53,412.40	61.80	33	30,342.60	64.00	39	21,594.50	59.30	56	41,713.20	61.00
Wells Fargo Bank	36	27,170.60	31.50	16	15,134.30	31.90	18	11,174.80	30.70	27	15,834.50	23.20
Deutsche Bank	4	2,913.60	3.40	2	1,966.90	4.10	2	946.70	2.60	9	7,141.10	10.40
USBank	8	2,894.00	3.30			0.00	7	2,685.40	7.40	6	3,112.60	4.60
Citibank										1	540.00	0.80
Total	**122**	**86,390.60**	**100.00**	**51**	**47,443.80**	**100.00**	**66**	**36,401.40**	**100.00**	**99**	**68,341.40**	

Source: Commercial Real Estate Direct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Republicans Notch a Major Win

By David McCarthy, Martin Schuh and Christina Zausner

Just before the holidays last year, the stars finally aligned to allow the 'governing' party to deliver on an oft-shouted, major campaign promise: tax reform.

The measure is being touted by the GOP as a huge stimulant to economic growth and worker wages, primarily through the massive headline reduction in corporate tax rates and temporary individual tax breaks (most provisions sunset after seven years).

After flailing on health care "Repeal & Replace" and the border wall, the Republicans were desperate for a win heading into the midterm election season this fall. Passing the tax bill will certainly give them a boost heading into a very challenging environment.

Looking Ahead: According to notable pundit Charlie Cook, midterm elections tend to be a referendum on the sitting president: The White House's party has lost ground in the House in 18 of the past 20 midterm elections, and in the Senate in 15 of those elections (e.g., 1994, 2006, 2010, 2014).

Timing Is Everything: It is always difficult summarizing regulatory and legislative events, and this year is even more difficult because there have been so many headlines with so little actual achievement. But as of Dec. 20, 2017, regulatory reform certainly seems more possible, although it may be more surgical than many in our industry would have liked.

Tax Reform Bill Highlights

The 2017 Tax Bill permanently lowers the corporate tax rate to 21 percent starting this year, restructures marginal rates on pass-through entities and small businesses and provides leveraged borrowers an option on their interest and cost recovery deductions.

The new interest deductibility restrictions broadly contained an exception for real estate businesses. However, the provision also allows for the immediate expensing of capital investments. Importantly, the bill also preserves Section 1031 Like-Kind Exchanges for real property.

As noted above, the legislation avoided major disruptions for long-term asset planning, but the personal side is far more uncertain due to staggered sunsets and unindexed thresholds that are sure to set up a series of legislative land mines for future Congresses.

Provisions for Business and Those Related to Commercial Real Estate

• Lowers the corporate tax rate to 21 percent from 35 percent, effective Jan. 1.

• Provides a deduction of 20 percent of qualified pass-through income, subject to certain tests.

• Allows businesses, for five years, to immediately write off the full cost of purchases of equipment and leasehold improvements (for buildings, however, real estate businesses have the option to choose between the current 39-year amortization or 40 years, depending on their preference for interest deduction).

• Protects the ability of real estate businesses, as well as small businesses or those with "floor plan" inventory financing, to write off loan interest.

• Retains the tax-preferred status of private-activity bonds.

• Includes "base-erosion" rules to prevent companies from hiding U.S. profits in offshore affiliates.

• Modernizes the international tax regime by moving to a "territorial" system.

• Returns overseas income through "deemed" repatriation.

Regulatory Headwinds Calm

What a Difference a Year Makes: Last year's annual report from the Financial Stability Oversight Council (FSOC) listed asset managers and commercial real estate as prime watch targets. In a significant about-face, 2017 ushered in a number of regulatory reform efforts, spurred in large part by the White House. Last year, both houses of Congress put forward major financial services regulatory reform bills; the Treasury Department published four reviews of regulations and statutes; and most recently, the FSOC published its annual report for 2017 naming "regulatory burden" in its executive summary as one of the major sources of risk for the financial system.

Early last year, the "big three" bank regulatory agencies — the Federal Reserve, FDIC and Office of the Comptroller of the Currency — published their *Economic Growth and Regulatory Paperwork Reduction Act* report, which identified potential regulatory revisions that included the High Volatility Commercial Real Estate (HVCRE) rule. While any revisions to capital rules would be put through lengthy public notice and comment, we expect action in the first half of the year.

The Prospects for Regulatory Reform Appear Modest, but Attainable

Two for One: One of President Trump's opening salvos aimed at the past administration was an executive order requiring that every new rule be accompanied by the repeal of two existing rules. That was followed by a series of leadership changes at the major regulatory agencies, which we estimate could yield turnover of roughly 75 percent of the principals at the agencies.

The rhetorical pendulum has swung for sure, but the effects may be relatively muted. Here's why:

• The repeal of existing rules and guidance is messy, if still feasible. Some repeals have been executed using the Congressional Review Act, (used in roughly a dozen instances across all sectors), or have been realized temporarily through delays. In sum, for all the bluster, this effort has yielded little in terms of permanent reforms.

• The Senate banking reform bill (S. 2155, the Economic Growth, Regulatory Relief and Consumer Protection Act) — in contrast to the House's CHOICE Act — covers only those changes supported by the Democrats and generally

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Retail Isn't a Dirty Word: Transformation Drives Opportunity

By Diane Crocker

Like the broader commercial real estate sector, the property due- diligence market is in transition due to its cyclical nature.

Transition due to the pressure of regulatory forces on lenders, and transition due to technological advances that are driving efficiency. Within this rapid transition is disruption — but also opportunity.

In perhaps no other asset class is this rapid change more pronounced than in retail. Consider a few stats:

• Retail is changing at its fastest pace since the introduction of the regional mall in the 1950s.

• Forty percent of U.S. retail centers will be obsolete by 2020.

• For every company closing a store, 2.7 are opening them.

• There were more than 4,000 net store openings last year, and another 5,500 are projected for this year.

Developments in retail last year went way beyond the dire headlines about record-high store closures. "Real estate investors forget that every 15 years or so, we blow up retail concepts and reinvent new ones," said KC Conway, director of research and corporate engagement at the University of Alabama. "A year in retail is like leap-year every year — four times as much change gets packed in because disruption is just more pronounced, given its direct link to the consumer. There is not an apocalypse in retail nor a decline in consumer spending."

The encouraging wrinkle is that disruption in retail is opening up opportunities to use space in a new way that is consistent with the changing demands of consumers in today's e-commerce culture. For anyone supporting property due diligence on retail assets or design work on site redevelopment, the retail glass is half-full.

ScoreKeeper Growth Rate (3Q17 vs. 3Q16)

Salt Lake City	4%
Pittsburgh	5%
San Jose, Calif.	-18%
Nashville, Tenn.	1%
Portland, Ore.	-12%
Fort Lauderdale, Fla.	-12%
Orange County, Calif.	8%
San Antonio	-11%
Seattle	5%
New York City boroughs	1%

Sources: ULI/PwC's Emerging Trends in Real Estate 2018 survey; EDR's ScoreKeeper model.

Opportunities to Redesign, Reuse, Remake Retail Properties

On a panel at a Commercial Real Estate Women Boston event last spring, Katy Gnapp, head of commercial real estate banking at Bank of America Merrill Lynch, said: "Retail is not overdeveloped. It's under-demolished." As retail properties trade, doors open for potential property re-use and value-add opportunities. Malls and old shopping centers are becoming mixed-use properties, medical centers, seniors housing or "power villages" if area demographics warrant.

Some successful e-commerce retailers started out exclusively online, only to realize the benefits of having physical locations. Meanwhile, opportunistic investors are taking advantage of bargain properties in good locations.

And traditional big-box retailers, like Target, are moving to smaller store footprints. Walmart Stores Inc. just changed its name to Walmart to get customers to think beyond its 11,700 store locations and offer more options to buy. There are strong capital flows into the grocery-anchored market. One of the most aggressive players today is Aldi, a German chain. According to GRS Group, a provider of commercial real estate services, Aldi's goal is to become the third-largest grocery chain in the U.S., by store count, within the next four years by adding 900 locations to its 1,300 existing locations, which it plans to remodel. German rival Lidl is set to open 100 U.S. stores by next summer, primarily on the East Coast. Those aggressive expansion plans are great news for the commercial real estate industry.

Continued on next page

Continued from page 32

makes extremely thin cuts to the existing framework. There is little in the Senate bill that would directly impact the CRE sector, save for a revision to the Home Mortgage Disclosure Act reporting thresholds that would modestly benefit very small banks.

The primary takeaway for CREFC is that as the new regulatory leaders take their seats, 2018 could be the year some of our member appeals are heeded by the agencies.

Other Legislative Issues for 2018

Hurry Up and Wait: Starting in mid-to-late January, the 2018 midterm elections will drive most of what is achievable out of Congress. Mindful of the Senate requirement that most all legislation must have 60 votes to overcome a filibuster, finding nine Democrats to side with the Republican majority will prove more than challenging. Outside of the usual push for reform of government-sponsored enterprises, and the Senate bill described above, we see little bipartisan opportunities in a year with so much at stake for both parties. But we do expect traction on the Senate regulatory bill, S. 2155, in the first quarter of the year. The bill's fate in the House, however, is less certain as the compromises struck in the bipartisan Senate negotiations could prove too moderate for the more conservative body. ■

David McCarthy is director supporting CREFC's policy and government relations team, Martin Schuh is senior director and head of government relations at CREFC and Christina Zausner is senior director and head of industry and policy analysis at CREFC.

Continued from previous page

Out With the Old Way of Doing Things, In With the New

As retail reinvents itself, it is creating significant momentum for transactions involving malls, shopping centers and single-store locations. The rise of e-commerce triggered retail's latest stage of evolution, but it is also changing how retailers conduct site selection and property due diligence.

"We are seeing a trend with our retail customers looking to couple business due diligence with environmental due diligence," explained Steve Long, principal-in-charge of environmental services with Intertek-PSI. "As a result, Intertek-PSI is working to offer our clients business analytics like traffic counts and retail sales metrics embedded in a geographic information system platform like our property risk data. We are also seeing more requests from retailers looking to perform early screening of multiple candidate properties at once."

The Era of "Risk-Off" Due Diligence is Here

The recession had a measurable impact on the way lenders and investors view property risk. Likewise, each year that passes brings us one year closer to the next cyclical downturn. As buyers and lenders get more cycle-aware, and as prices level out in some metropolitan areas and some asset classes, deals aren't the slam-dunks they may have been a few years ago.

The era of "risk-off" due diligence has arrived. A $2 million shopping center today may not be worth that much a few years down the road, and there is a slimmer margin for error in assessing a property's risk profile. Buyers are looking for ways to protect themselves in the event of a market slowdown, but in retail, the interest in buying well-positioned properties is there.

"Demand by investors continues to be strong, as developers have been able to obtain more favorable lease terms," observed Noreen Clindinning, president of GRS Group. "The franchise restaurant and retail space continues to see heightened interest … Consolidation also continues, as owners seek to gain market share and territories from smaller franchisees."

In terms of geographic hot spots for retail properties, the *ULI/PwC's Emerging Trends in Real Estate* report puts Salt Lake City, Pittsburgh and San Jose, Calif., in the top three (see page 34). EDR's ScoreKeeper model tracks environmental due-diligence activity (measured in terms of the volume of Phase I environmental site assessments) for the U.S. market, states and metros.

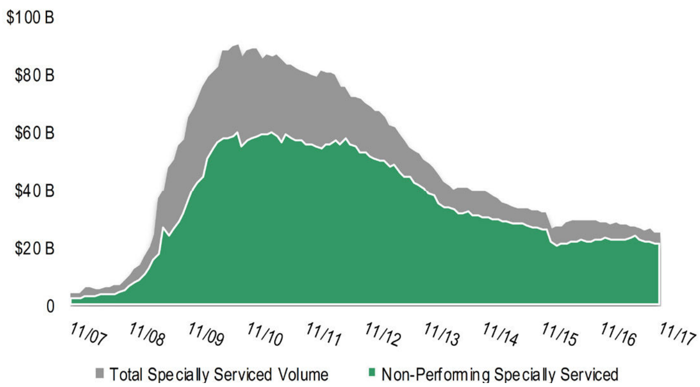
Since due diligence is performed prior to a property transaction, Phase I environmental site assessment activity is a leading indicator of commercial real estate investment activity. The retail magnets in the ULI/PwC ranking that were already seeing strong demand for site assessments in the third quarter were Orange County, Calif., Seattle and Pittsburgh. If the ULI/PwC prediction is accurate, current slow performers like San Jose, Portland, Ore., and Fort Lauderdale, Fla., may have cause for optimism this year.

Strong demand for evaluating retail sites for investment and reuse are ahead as the lines blur between e-commerce and traditional brick-and-mortar stores, and as new technologies change the old ways of looking at property risk efficiently — not just in retail, but in other asset classes as well. ■

Dianne Crocker is principal analyst at EDR Insight, the analytical arm of EDR, a national provider of data, risk-management and technology tools and insight for property due diligence and compliance.

The Data Digest

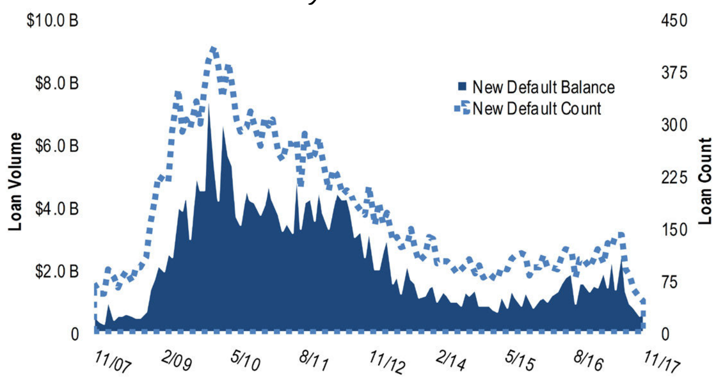
Special Servicer Volume



Source: Trepp LLC

The volume of CMBS loans in special servicing totaled $24.49 billion as of November. That's down from $28.14 billion a year earlier.

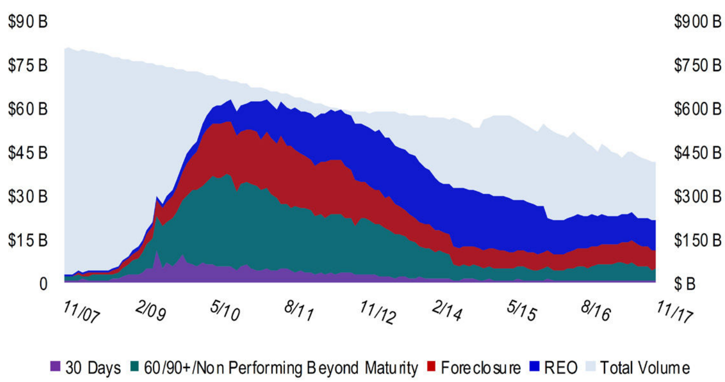
Monthly New Defaults



Source: Trepp LLC

Last year, an average of $1.42 billion of loans defaulted every month. That was up from the $1.37 billion monthly average in 2016.

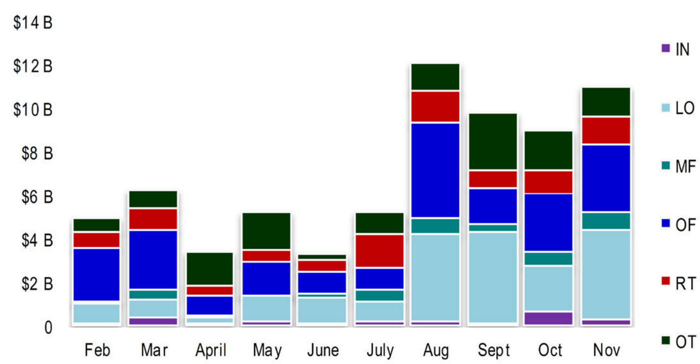
Delinquency Breakdown



Source: Trepp LLC

A total of $21.2 billion of CMBS loans were delinquent as of the end of November, down from $22.7 billion a year earlier and $26.4 billion in 2015. Every delinquency category has improved since the start of last year. The volume of loans classified as more than 60-days, but less than 90-days late dropped by almost 30 percent to $638.1 million.

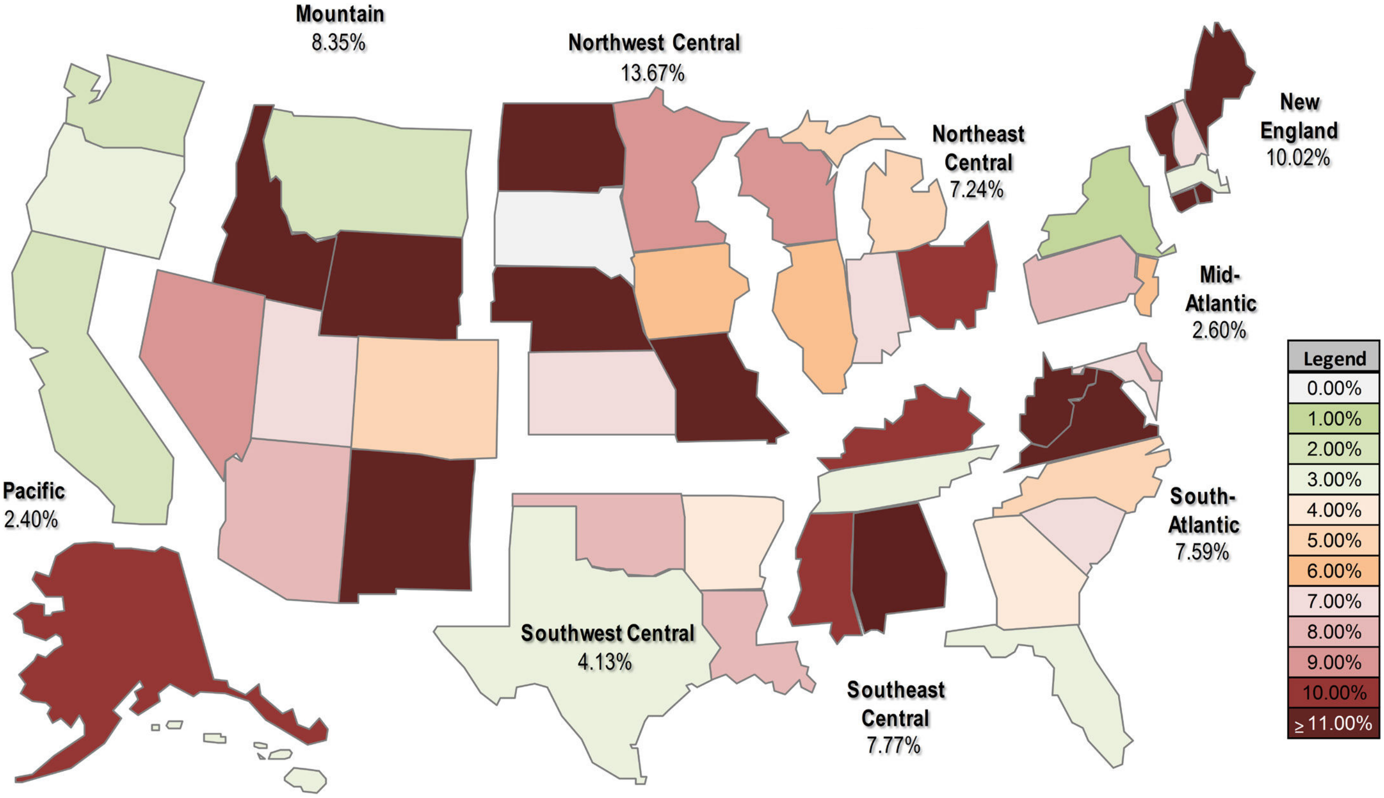
2017 CMBS Issuance



Source: Trepp LLC

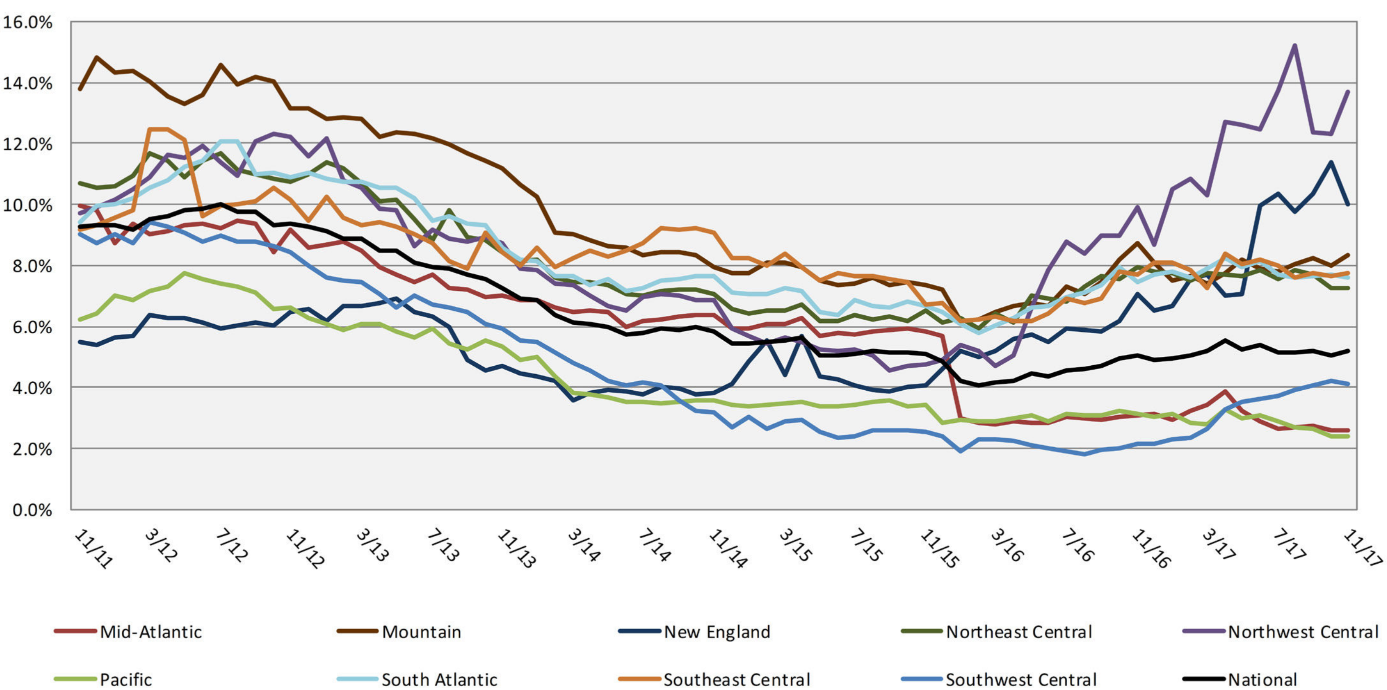
A total 14.4 percent, or $9.4 billion, of the CMBS issued last year backed retail properties. Office loans represented about one-third of the collateral for the year's deals, and hotels comprised about 30 percent.

Delinquencies by State and Region



Source: Trepp LLC

Delinquencies by Region



Source: Trepp LLC

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