Not all is Lost: Average Losses for CMBS Loans Down Markedly Since 2011

Coming out of the economic recession in 2009, a considerable number of securitized mortgages backed by US commercial properties paid off with extensive losses in the early years of the recovery. Since 2010, over $400 billion in non-agency CMBS loans paid off or were disposed with losses, amounting to cumulative losses of over $36.2 billion for the industry as a whole. As real estate values rebounded and property-level growth in occupancy and NOI levels boosted the performance of maturing CMBS loans during this time period, losses on liquidated loans fell significantly across all property sectors and metropolitan regions.

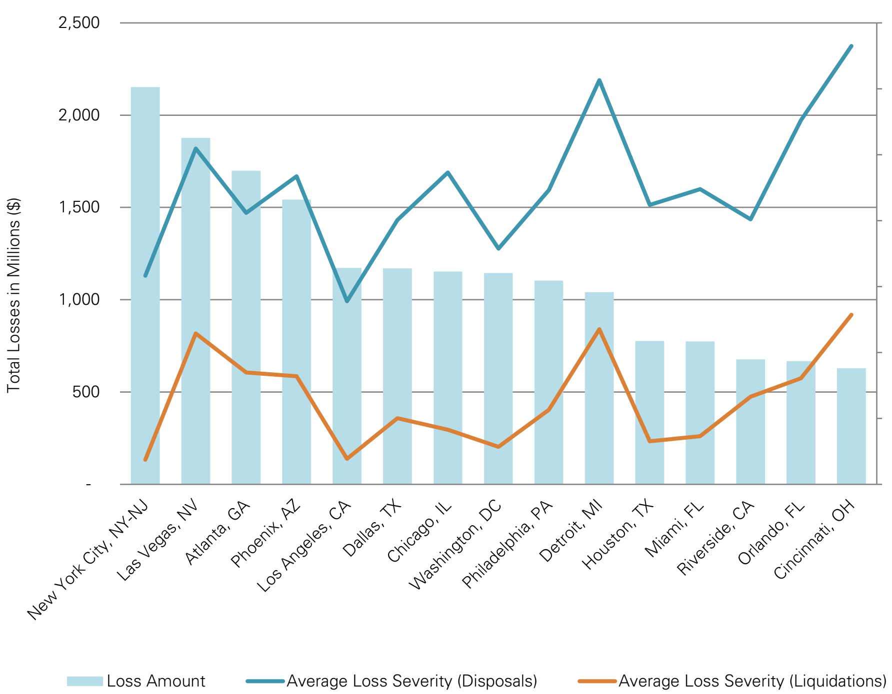
When looking at a yearly basis, loss percentages for all loans that paid off reached a peak of 14.15% in 2011. Since then, that number has dipped to 4% for loans liquidated in January 2015 or after. For loans that resolved in 2016, the average loss severity has declined consistently in the past three quarters, falling from 6.41% in the fourth quarter of 2015 to 2.31% in the third quarter of 2016. While total sector losses declined as the share of troubled loans started to plummet, the average loss severity for loans that were written off with losses has remained relatively steady throughout the years, fluctuating within the low- to mid-40% range.

In this analysis, Trepp examines losses reported on US CMBS loan liquidations that took place between January 2010 and September 2016. Broken down by metropolitan statistical area (MSA) as defined by the Office of Management and Budget (OMB) and property type, the losses reflect data on private label, fixed-interest mortgages securitized between 1996 and 2015. (As of the end of September 2016, no loans issued in 2016 have taken a loss.) Total losses recorded for each category are a reflection of resolution activity and overall market conditions in each sector analyzed, as well as the profile of the individual loans that paid off.

In measuring losses by MSA and property type, we frame losses for these segments in terms of loans that have just taken losses and for all loans that have been paid off in any manner. For the purpose of distinguishing the two groups of loans, we refer to each as the following:

- Liquidated loans: loans that have been resolved via any method (full payoff, paid post maturity, loss, etc.)
- Disposed loans: just loans that have been paid off with a loss

Figure 1: MSAs with the Highest Cumulative Losses 2010-2016 YTD



Source: Trepp

When a loan is disposed, the total sum of the write-off is called the loss amount. When you measure the loss amount against the loan balance at the time of disposal, a percentage is calculated called the loss severity. (For instance, a $5 million loss incurred by a $10 million loan will yield a 50% loss severity.) The data in this report references the total amount of losses incurred by disposed loans by property type and MSA, and that will be put against each sector's total disposed and liquidated balances

Aggregate Losses by MSA: 2010 – 2016 YTD

Typically, heavily populated metropolitan areas with a large commercial real estate footprint will receive high CMBS origination volume and activity. The New York-Newark-Jersey City MSA is the largest in the US, so it's not terribly surprising that it incurred the largest volume of losses by MSA over the time period analyzed.

In terms of cumulative dollar losses for all liquidated securitized loans, the New York City-Newark-Jersey City MSA topped the rankings with over $2.2 billion in total losses. As the most populous metropolitan area in the US, the New York City MSA boasts one of the strongest real estate sectors in the world thanks to stable property values and occupancy rates.

3,379 CMBS loans backed by NYC area properties totaling $57.6 billion have been liquidated since 2010, the highest respective totals amongst all MSAs. Just 3.74% of that aggregate balance was wiped out via loan losses. Out of the 312 loans backed by NYC area properties that were disposed with losses, average loss severity totaled 31.63%.

Not far behind NYC is the Las Vegas-Henderson-Paradise MSA with roughly $1.9 billion in total realized losses. The Las Vegas economy and housing market was one of the hardest hit by the economic recession as large scale job cuts caused borrowers to default on mortgage payments. With many loans falling underwater and property foreclosures increasing in number after the housing crisis, a large amount of capital began flowing into Las Vegas' distressed housing market following the recession. While regional property valuations have partially bounced back throughout the recovery, values still generally fall below peak levels.

679 loans behind Las Vegas properties were liquidated in the time period measured, and the average loss severity for those notes clocks in at 22.88%. 292 loans from the Las Vegas metropolitan area were disposed with losses at an average loss severity of 50.95%.

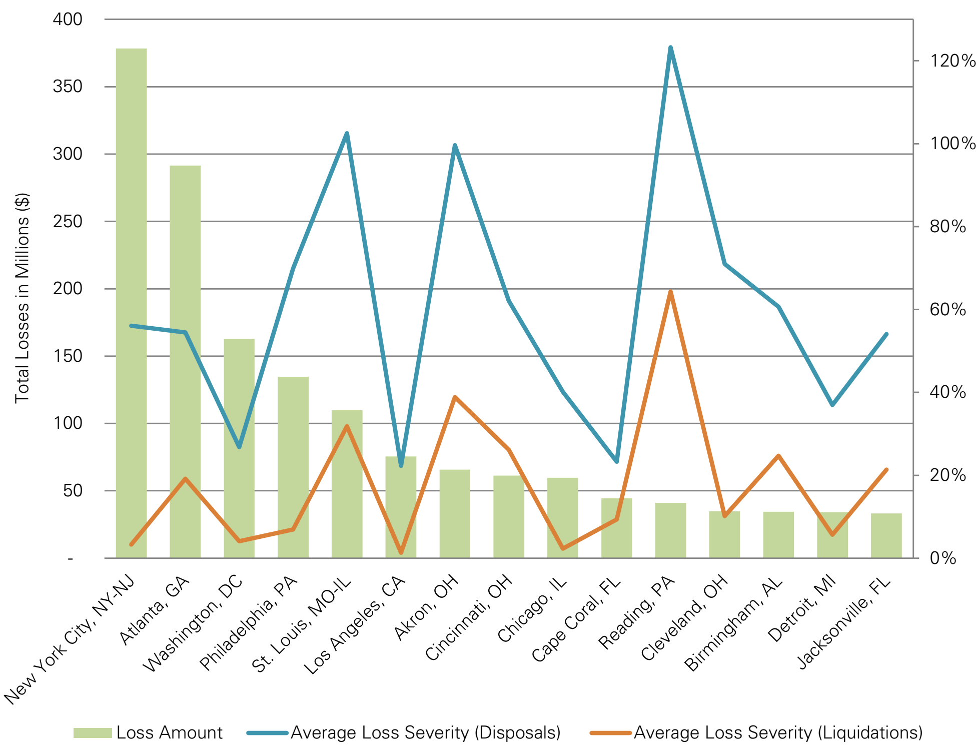
Among the 15 metropolitan regions with the highest cumulative dollar losses since 2010, the Cincinnati MSA finished at the top of several categories. The Cincinnati region was tagged with the highest average loss severity among the top 15 MSAs when looking at all liquidated and disposed loans. Coupled with a sluggish economy and slow population growth following the economic downturn, heavy construction activity in the years leading up to the housing crisis resulted in an excess of housing supply that later translated to

Figure 2: Total Losses by MSA 2010-2016 YTD

MSA	Cumulative Losses ($)	Loss Severity (Disposals)	Loss Severity (Liquidations)	Avg. Loan Size ($)	Loans Disposed w/ Loss (%)
New York, NY-NJ-PA	2,152,786,030	31.63%	3.74%	17,050,575	9.23%
Las Vegas, NV	1,876,923,394	50.95%	22.88%	12,080,620	43.00%
Atlanta, GA	1,698,561,143	41.17%	16.95%	10,059,429	38.25%
Phoenix, AZ	1,542,903,292	46.71%	16.38%	9,327,091	34.16%
Los Angeles, CA	1,171,935,939	27.75%	3.85%	11,284,490	8.75%
Dallas, TX	1,169,366,147	40.09%	10.03%	9,176,415	22.66%
Chicago, IL -IN-WI	1,153,305,272	47.30%	8.26%	14,659,425	24.26%
Washington, DC-VA-MD-WV	1,144,900,895	35.75%	5.69%	17,570,152	12.66%
Philadelphia, PA-NJ-DE-MD	1,103,527,151	44.65%	11.30%	12,713,703	18.23%
Detriot, MI	1,040,836,274	61.30%	23.53%	7,870,629	37.72%

Source: Trepp

Figure 3: MSAs with the Highest Cumulative Losses (2016 YTD)



Source: Trepp

declining property values and rising mortgage defaults. All of these factors have kept Cincinnati real estate prices from growing above the national average.

256 area loans totaling $2.44 billion in CMBS loans were liquidated in any fashion. There was $628.5 million in losses tied to those notes, amounting to an average loss severity of 25.7%. Of the 64 notes that were disposed with losses, the average loss severity incurred by these mortgages came to 66.5%.

Figures 1 and 2 showcase the 15 MSAs that have accumulated the highest total losses based on CMBS loan liquidations since 2010. To exclude loans that may contain CMBS exposure across more than one MSA, portfolio loans secured by properties spanning several counties were removed.

2016 YTD Loss Standings

When looking at the first nine months of 2016, the New York City MSA is once again at the top of the loss chart. 465 loans backed by area properties have been liquidated through the first three quarters of 2016 with an average loss severity of 3.29%. Out of that loan total, 40 notes were disposed with losses averaging 56.06% in severity. The Atlanta-Sandy Springs-Roswell metropolitan area, which ranks third in total losses accrued since 2010, is not far behind with $291.4 billion in losses across 122 loans for 2016. 20 of those notes were disposed with an average loss severity of 54.46%,

Figure 4: Total Losses by MSA 2016 YTD

MSA	Cumulative Losses ($)	Loss Severity (Disposals)	Loss Severity (Liquidations)	Avg. Loan Size ($)	Loans Disposed w/ Loss (%)
New York, NY-NJ-PA	378,366,888	56.06%	3.29%	24,712,519	8.60%
Atlanta, GA	291,389,664	54.46%	19.17%	12,457,580	16.39%
Washington, DC-VA-MD-WV	162,801,254	26.81%	4.08%	21,914,033	12.64%
Philadelphia, PA-NJ-DE-MD	134,649,388	69.86%	6.93%	15,667,313	12.10%
St. Louis, MO-IL	109,728,324	102.53%	31.84%	11,116,380	12.90%
Los Angeles, CA	75,508,420	22.30%	1.32%	13,558,493	3.56%
Akron, OH	65,811,350	99.63%	38.87%	12,094,392	14.29%
Cincinnati, OH-KY-IN	61,233,650	62.11%	26.18%	6,322,585	21.62%
Chicago, IL-IN-WI	59,722,906	40.11%	2.29%	15,283,389	11.70%
Cape Coral-Fort Myers, FL	44,387,474	23.26%	9.36%	47,399,955	10.00%

Source: Trepp

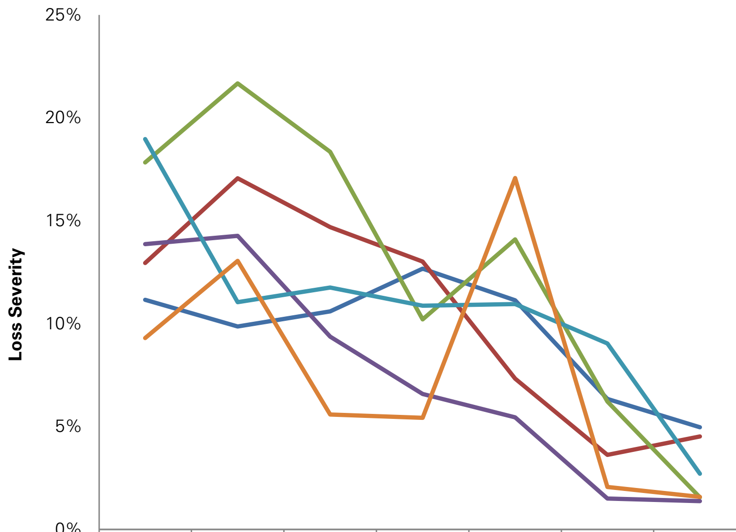
Of the ten metropolitan areas with the largest loss totals for the year thus far, the highest average loss severity for liquidations belonged to the Akron, Ohio MSA at 38.87%. In terms of disposals, the St. Louis MSA featured the highest average loss severity with a whopping 102.53%. These two markets, along with Atlanta, feature notes collateralized by area properties that were disposed with some of the largest individual loan losses of 2016 so far.

Among the conduit loans hit with the heaviest losses in the past three quarters, the $363 million Bank of America Plaza incurred the largest loss by dollar amount. The loan was backed by a 1.3 million square-foot office tower in Atlanta that suffered from low occupancy and DSCR levels due to high vacancies in the Midtown Atlanta submarket. The REO asset was eventually sold to Shorenstein Realty in January for an undisclosed amount, while the loan was disposed with a 55.66% loss severity. Rounding off the list of the five loans with the highest loss amounts for 2016 thus far are the $225 million Riverton Apartments (49.98% severity), the $77.5 million St. Louis Mills (98.24% severity), the $88 million Continental Plaza (84.2% severity), and the $65.2 million Chapel Hill Mall (100% severity).

Losses by Property Type

Looking at losses based on property type, we can infer that certain property sectors are particularly sensitive to economic slowdowns, while others bounce back more quickly amidst improving market conditions. Since 2010, lodging loans have suffered the highest average loss severity for liquidated loans among all major property types. Cost-cutting measures were adopted by businesses and households to minimize spending on travel following the recession, which drove hotel occupancies and daily room rates down. The decline in tourism activity eventually caused the lodging delinquency rate to reach an all-time high of 19.46% in September 2010, a 12.87% increase from the same period a year before. Between 2010 and 2012, losses on liquidated lodging loans peaked at an average severity of 19.29%. As tourism increased and the delinquency rate returned to single digits in 2013, the hospitality sector began to face growing competition from sharing-based lodging alternatives

Figure 5: Loss Severity by Property Type (Liquidations)



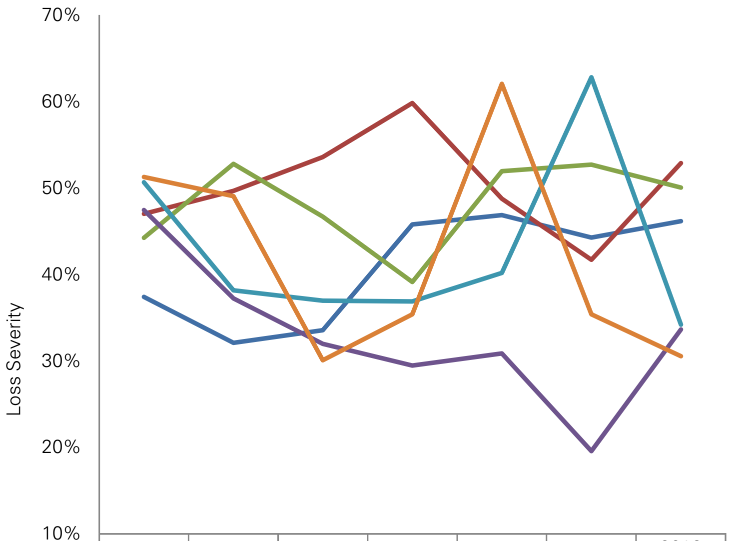
	2010	2011	2012	2013	2014	2015	2016 YTD
OF	11.16%	9.86%	10.60%	12.67%	11.14%	6.35%	4.97%
RT	12.95%	17.07%	14.69%	13.02%	7.33%	3.63%	4.52%
LO	17.83%	21.67%	18.35%	10.21%	14.09%	6.22%	1.56%
MF	13.87%	14.26%	9.38%	6.58%	5.45%	1.50%	1.38%
IN	18.97%	11.05%	11.75%	10.87%	10.95%	9.04%	2.71%
OT	9.30%	13.05%	5.59%	5.43%	17.07%	2.07%	1.59%

Source: Trepp

like Airbnb and HomeAway. Even with some loss of potential business, recent hotel performance and overall fundamentals have been strong as the average loss severity for liquidated lodging CMBS loans was just 3.89% from the start of 2015 through the first three quarters of 2016. However, loss severity remains elevated when looking at loan disposals, as the average loss severity for those notes has been above 50% over the last 21 months.

Liquidated loans backed by multifamily properties have incurred the lowest average loss severity since 2013. Although loss percentages rose to double digits between 2010 and 2011, the average severity dipped below 2% in 2015 and 2016, partly due to the resolution of the $3 billion Stuyvesant Town/Peter Cooper Village Complex loan without a loss. Split into five CMBS loan pieces across five different deals, the debt was liquidated between December 2015 and January 2016. The StuyTown loan was a rare case: Blackstone agreed to purchase the foreclosed apartment complex for $5.3 billion, which allowed the mortgage to be paid off with no losses despite spending nearly six years in default. In the past 21 months (ever since

Figure 6: Loss Severity by Property Type (Disposals)



	2010	2011	2012	2013	2014	2015	2016 YTD
OF	37.41%	32.08%	33.56%	45.77%	46.87%	44.25%	46.15%
RT	47.00%	49.65%	53.57%	59.81%	48.74%	41.68%	52.88%
LO	44.24%	52.77%	46.67%	39.12%	51.94%	52.69%	50.03%
MF	47.45%	37.21%	31.98%	29.46%	30.86%	19.56%	33.63%
IN	50.67%	38.17%	36.95%	36.88%	40.17%	62.80%	34.20%
OT	51.28%	49.05%	30.06%	35.39%	62.03%	35.39%	30.53%

Source: Trepp

the StuyTown resolution), multifamily losses averaged 2.56% across all liquidated notes (when the Stuytown loan is excluded from the calculation) and 23.21% for all loans that were resolved with losses.

Loan losses across all major property sectors fell from 2013 to the end of 2014, with the largest decline by percentage observed in liquidated loans backed by retail properties. However, retail was the only property type that underwent an increase in sector losses between 2015 and 2016YTD thanks to the continued expansion of e-commerce altering the retail landscape. The retail sector recorded the highest average loss severity of all loans disposed with a loss in the first three quarters of 2016 at 52.88%. Aided by growing demand for warehousing and an industry-wide shift towards smaller physical footprints at brick-and-mortar locations, the average loss severity for industrial loans has also decreased substantially since 2010, falling from 9.04% in 2015 to 2.71% in 2016 YTD.

Outlook

Looking forward, losses based on property type and metropolitan region will continue to be shaped by prevailing real estate trends and local market performance driven by macroeconomic factors. Of the roughly $160 billion in CMBS debt slated to mature from now until the end of 2018, around 11.5% of that balance is currently seriously delinquent (60+ days delinquent, REO, foreclosed, or non-performing beyond maturity). About 14.4% has been transferred to special servicing. For loans scheduled to mature in the last quarter of 2016, 40.1% are 60+ days past due on payment, while 43.27% have been sent to special servicing. However, the overall outlook on the ability of these loans to refinance at maturity (or to minimize losses at liquidation) appears favorable given the strong demand and property level fundamentals observed in the current CRE environment.

For inquiries about the data analysis conducted in this research, contact press@trepp.com or call 212-754-1010. For more information on Trepp's products, contact info@trepp.com.

About Trepp

Trepp, LLC, founded in 1979, is the leading provider of information, analytics and technology to the CMBS, commercial real estate and banking markets. Trepp provides primary and secondary market participants with the web-based tools and insight they need to increase their operational efficiencies, information transparency and investment performance. From its offices in New York, San Francisco and London, Trepp serves its clients with products and services to support trading, research, risk management, surveillance and portfolio management. Trepp is wholly-owned by DMGI, the information publishing division of the Daily Mail and General Trust (DMGT).