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Trepp®

CRE Research

Retail Round-Up: Loan Losses Rise as Bankruptcies Mount

In light of the large wave of bankruptcies and store closures that have hit the retail sector since 2016, Trepp will publish the following retail recap every month in an effort to monitor the current retail CMBS environment.

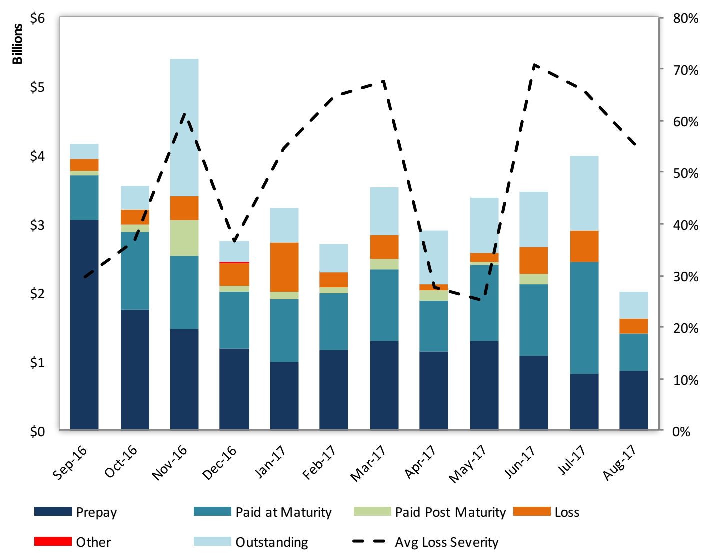
The term "retail apocalypse" has made its way into the commercial real estate lexicon in the past two years as a result of the mass closings of thousands of brick-and-mortar retail stores across the United States. In an increasingly digitized world, traditionally well-established retailers like Macy's, JCPenney, and Gordmans have commented that the modern retail landscape – now characterized by ecommerce and transformed consumer trends – has led to declining sales figures and disappointing earnings results in recent fiscal quarters. For the retail sector in CMBS, the departure of major big box anchors from retail centers has caused a significant number of loans to fall into distress.

Since 2016, there has been an uptick in the percentage of retail loans that have defaulted on payment or been sent to special servicing. It shouldn't surprise many market followers that rates for troubled loans have been trending upwards in conjunction with the large volume of CMBS maturities that have come due over the last few years. A considerable share of these retail loans fell into maturity default as they inched closer to their balloon dates and struggled to secure refinancing. In particular, lending towards malls and shopping centers have been subject to increased scrutiny and caution in the past two years due to the general retail malaise that has swept over the sector, leading to a sizable reduction in the share of retail loans in the 2017 issuance pipeline compared to previous years.

Retail CMBS Performance

In the 12-month period between September 2016 and August 2017, roughly $33.3 billion in securitized mortgages backed by retail properties were paid off or liquidated, 10.92% of which incurred losses at resolution. These loans that were disposed with losses were written off at an average loss severity of 54.54%, resulting in a 5.95%

GRAPH 1: RETAIL CMBS – PAYOFFS FROM LAST 12 MONTHS

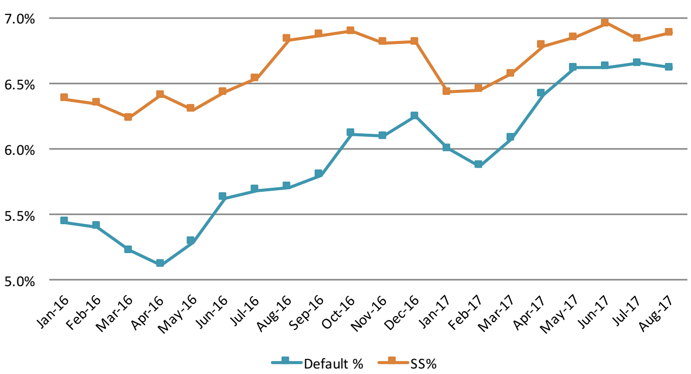


Source: Trepp

loss on the total balance of all retail loans that paid off. In comparison, the overall CMBS loss severity for loans disposed within that time frame was just 43.66%. Based on underwritten maturity dates for loans that were scheduled to pay off during this time frame, $8.3 billion across 500 retail loans are still outstanding. Total liquidation volume from the retail loans for the month of August reached $1.92 billion, while average loss severity for loans disposed with a loss came in at 55.43%. Backed by a 564,410 square-foot regional mall in Richmond, California, the $64.4 million Hilltop Mall loan took on the highest losses out of all retail dispositions with a 78.16% loss severity.

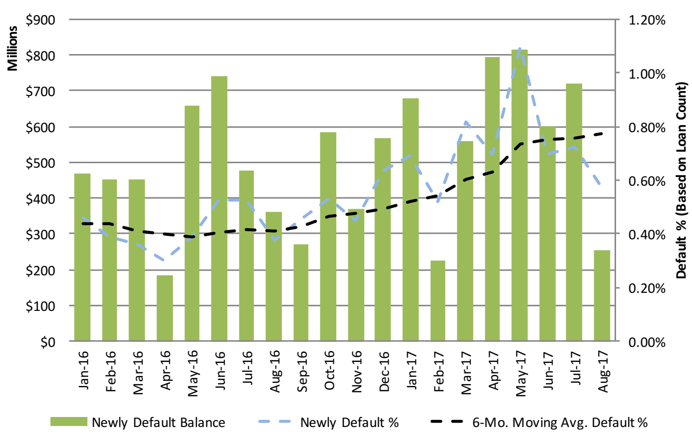
In Trepp's analysis, default rates were calculated by taking the total number of retail loans that have entered default every month and dividing that by the total number of

GRAPH 2: RETAIL CMBS – SPECIAL SERVICING TRANSFER AND DEFAULT RATES



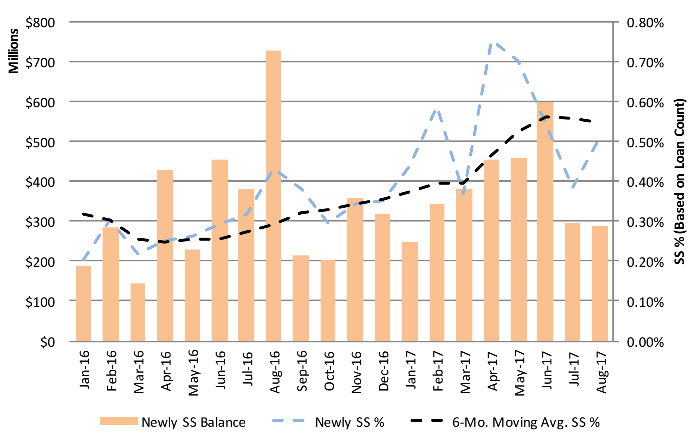
Source: Trepp

GRAPH 3: RETAIL CMBS – NEWLY DEFAULTED RATES



Source: Trepp

GRAPH 4: RETAIL CMBS – SPECIAL SERVICING TRANSFER RATES



Source: Trepp

loans that were not categorized as being in default in the previous month. To us, default is defined as loans that are 60+ days delinquent, in foreclosure, REO, or considered to be non-performing balloons. Similarly, the percentage of loans that are newly transferred to special servicing is calculated by taking the total count of loans that were transferred to special servicing in the present month as a numerator, and using the total number of loans that were not in special servicing in the month prior. Total loan count was used in this study rather than outstanding loan balance to give equal weight to each retail transaction, regardless of asset size.

Newly Defaulted Retail Loans:

- In the month of August, 38 loans with a remaining balance of $254.8 million entered default at a default rate of 0.57%. This is 15 basis points lower than July's rate of 0.72%.
- The six-month moving average default rate, which can be used as an indicator of prevailing trends, climbed 23 basis points from 0.54% in February 2017 to 0.77% in August.
- The largest loan that fell into default in August was the $33 million City Center Englewood note, which represents 23.03% of the remaining collateral behind BSCMS 2007-PW17. The subject property is a 218,076 square-foot, community shopping center in Englewood, Colorado anchored by such retailers as Ross Dress for Less, 24-Hour Fitness, and Office Depot. The loan was designated as a non-performing matured balloon in August, and was previously transferred to special servicing in June 2017 for imminent maturity default.
- The percentage of retail loans in default fell from 6.65% in July to 6.62% in August. The CMBS default figure for all property types clocked in at 5.43% for August, down from a reading of 5.48% in July.

Newly Transferred to Special Servicing:

- In August, 34 loans totaling $287.7 million were sent to special servicing. This amounts to a special

- servicing transfer rate of 0.51%, up 13 basis points from July.

- The six-month moving average rate of special servicing transfers clocked in at 0.55% for August, which is up 16 basis points from the six-month average measured in February 2017.

- The largest loan that was transferred to special servicing last month was the $29.4 million Cole Centerpointe of Woodridge note. The loan was tagged with an imminent default due to the potential departure of main tenants JCPenney, Sam's Club, and Home Depot. The anticipated repayment date (ARD) loan, which is backed by a 466,426 square-foot regional mall in Woodridge, Illinois, comprises 3.90% of the outstanding balance for WBCMT 2007-C33 and received a 10-year maturity extension to February 2027 earlier this year.

- About 6.88% of the total retail CMBS universe was in special servicing in August, up five basis points from 6.83% in July. The percentage of CMBS loans in special servicing for all property types dipped six basis points from 6.45% in July to 6.39% in August.

Recent Retail Headlines:

- **Aerosoles:** Women's footwear retailer Aerosoles filed for chapter 11 bankruptcy on September 15th and indicated that it plans to downsize a significant portion of its current physical footprint. Aerosoles representatives expect the retailer to emerge out of bankruptcy after a four-month restructuring period.

- **Amazon/Whole Foods:** Amazon's acquisition of Whole Foods for a record $13.7 billion stirred up major concerns among its brick-and-mortar competitors in the grocery sector. After the merger became finalized in late August with official approval from the FTC, the *Wall Street Journal* reported that several Whole Foods locations noticed an increase in sales and foot traffic after price cuts were introduced to many of its popular product offerings. Not surprisingly, the announcement of Amazon's price discounts battered stocks of other food retailers like Kroger, SuperValu, Target, Sprouts Farmers, and Costco, initially erasing billions of dollars in market value from the grocery segment.

- **Bed, Bath, & Beyond:** Following disappointing first quarter earnings results, Bed, Bath, & Beyond revealed in August that it was gearing up to close a dozen Buy Buy Baby locations and lay off 880 store managers to reduce operating costs and reorganize its current management structure. The domestic merchandise retailer is looking to renegotiate rent terms for expiring leases and will consider closing up to 100 stores in the coming years.

- **Bon-Ton:** Bon-Ton Inc. recently hired a restructuring firm to explore potential bankruptcy options to tackle its debt load of more than $900 million. Bon-Ton also

CHART 1: METROPOLITAN STATISTICAL AREAS WITH THE LARGEST EXPOSURE OF RETAIL CMBS IN DEFAULT

CBSA NAME	RETAIL DEFAULT BALANCE	TOTAL RETAIL EXPOSURE	WALTV*	WADSCR*	AVG. OCCUPANCY*
Las Vegas-Henderson-Paradise, NV	$330,118,006	$4,850,249,695	59.09%	2.10	93.80%
New York-Newark-Jersey City, NY-NJ-PA	$309,516,390	$12,776,956,189	59.68%	2.34	97.12%
Chicago-Naperville-Elgin, IL-IN-WI	$284,637,132	$3,027,411,459	65.13%	1.73	96.04%
Phoenix-Mesa-Scottsdale, AZ	$272,540,018	$2,291,344,047	62.52%	1.86	93.20%
Atlanta-Sandy Springs-Roswell, GA	$239,867,749	$2,624,009,576	70.12%	1.87	93.07%
Riverside-San Bernardino-Ontario, CA	$237,776,754	$2,154,426,673	63.64%	1.95	94.01%
Kansas City, MO-KS	$232,268,885	$582,379,158	66.98%	1.55	96.22%
St. Louis, MO-IL	$226,774,841	$988,145,988	56.01%	2.78	95.53%
Pittsburgh, PA	$223,775,287	$756,854,153	68.52%	1.87	97.64%

**WALTV, WADSCR, and average occupancy columns are based on most recently reported values for all current, fixed-rate securitized retail loans* serves as the parent company that owns and operates a number of other retailers such as Elder-Beerman, Boston Store, Carson's, Herberger's, and Younkers.

- **Gymboree:** The San-Francisco based children's clothing chain is expected to finalize restructuring plans after filing for bankruptcy protection back in June. Gymboree is preparing to liquidate 330 underperforming stores and will be wrapping up a recapitalization effort that would minimize its total debt balance by $900 million.

- **Neiman Marcus:** Due to sluggish sales, the luxury retailer will be closing 10 of its 38 discount outlet stores that it currently operates under the "Last Call" umbrella. Instead, Neiman Marcus will evaluate the option to focus more on its high-end luxury lines through its Neiman Marcus and Bergdorf Goodman channels.

- **Perfumania:** The New York-based perfume retailer filed for bankruptcy protection on August 23rd in a restructuring effort to reduce costs and seek strategic business alternatives. In addition to making the shift to a private entity, the company will also be shuttering roughly 65 locations nationwide, which accounts for roughly one quarter of its 226-store portfolio, as it focuses on growing its online presence. The underperforming locations that are slated for closure have not been disclosed.

- **Rue21:** Rue21, which petitioned for bankruptcy in mid-May, is in the process of emerging out of bankruptcy protection less than four months after gaining formal clearance on a new reorganization plan. The teen apparel brand has operations in 48 states and closed around 421 stores while it was in bankruptcy.

- **Toys "R" Us:** Similar to other retailers that are grappling with a significant amount of debt coming due within the next two years, Toys "R" Us hired law firm Kirkland & Ellis to strategize on how to resolve its $5 billion debt loan, $400 million of which is slated to mature by 2018. After reporting a net loss of $164 million in Q1 2017 due to sluggish sales in its critical Babies "R" Us business line, Toys "R" Us formally filed for bankruptcy protection on September 15th. While the retailer indicated that the bankruptcy should not affect its operations nationwide as the "vast majority" of its stores still remain profitable, it is likely that Toys "R" Us will be evaluating its current physical presence during the bankruptcy process.

- **Vitamin World:** In a chapter 11 bankruptcy filing that was submitted on September 11th, Vitamin World identified 51 of 334 stores that the specialty retailer has flagged for closure. Citing expensive leasing terms and supply disruptions as the main cause for seeking bankruptcy protection, the retailer will be working to lower its $44 million debt load.

CHART 2: CMBS EXPOSURE OF TROUBLED RETAILERS (WHEN LISTED AS TOP FIVE TENANT):

RETAILER	LOAN BALANCE	LOAN COUNT	AVERAGE OCCUPANCY	WADSCR*	AVERAGE DSCR
Bon-Ton	$1,322,852,035	26	107,358,000	91	1.99
Bergner's	$27,446,366	1	-	71	1.46
Elder-Beerman	$254,280,480	12	51,103,614	93	1.24
Boston Store	$123,859,246	3	-	97	1.49
Carson's	$1,354,413,832	12	-	97	2.20
Herberger's	$437,957,816	12	10,473,121	93	3.03
Younkers	$352,230,323	7	99,680,722	90	2.00
Bed, Bath, and Beyond	$8,072,152,036	219	356,792,541	94	1.95
Rue 21	$670,977,086	48	26,387,474	92	1.68
Toys "R" Us/Babies "R" Us	$5,569,370,905	114	165,904,651	94	1.92

**Excludes large portfolio loans backed by more than 5 properties*

For inquiries about the data analysis conducted in this research, or for more information about Trepp's commercial real estate data, contact info@trepp.com or 212.754.1010.

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About Trepp

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