CMBS Alert

Bon-Ton Rings Up 40 Store Closures--$416.0 Million in CMBS at Elevated Risk

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Morningstar Perspective

Morningstar Credit Ratings, LLC sees elevated risk in $416.0 million in loans on properties backing securitized commercial mortgages, after The Bon-Ton Stores, Inc. announced plans to shutter 40 of its 260 stores through year-end 2018. Although the retailer didn’t specify which stores are slated for closure, we identified the 14 riskiest loans as those already in distress or those with leases expiring before year-end 2020 with either a debt service coverage ratio below 1.25x or a collateral vacancy rate that would fall below 80% if Bon-Ton were to vacate, as displayed in Table 1. Overall, there are 59 loans with an allocated property balance of $2.38 billion in commercial mortgage-backed securities with exposure to one of Bon-Ton’s branded stores. Morningstar cautioned in an August Alert that the Milwaukee and York, Pennsylvania-based Bon-Ton, which also operates stores under the names Boston Store, Younkers, Bergner's, Carson Pirie Scott, Elder-Beerman, and Herberger's in the Midwest, Northeast, and upper Great Plains, would likely be closing stores.

Table 1 –Bon-Ton Loans of Concern

Deal ID	Property Name	City	State	Allocated Property Balance ($)	Property Balance (% of Deal)	Percent of Net Rentable Area (%)	Occupancy (%)	Occupancy Without Bon-Ton (%)	Lease Expiration	Debt Service Coverage Ratio (x)
JPMBB 2013-C14 &	Southridge Mall*	Greendale	WI	71,750,219	7.2	N/A	96.0	N/A	N/A	1.58
JPMBB 2013-C12				47,833,479	4.1					
LBCMT 2007-C3	University Mall	South Burlington	VT	92,000,000	44.0	9.8	99.0	89.2	1/31/2020	0.96
GSMS 2014-GC18	Wyoming Valley Mall	Wilkes-Barre	PA	75,081,496	7.2	17.1	92.0	74.9	12/6/2023	1.06
COMM 2014-CR14 &	McKinley Mall	Buffalo	NY	26,355,910	2.0	13.4	92.0	78.7	7/5/2023	1.29
COMM 2014-LC15				9,412,825	1.1					
COMM 2012-LC4	Susquehanna Valley Mall	Selinsgrove	PA	25,854,316	3.4	14.3	81.0	66.7	1/31/2020	1.50
WFRBS 2011-C4	Wausau Center*	Wausau	WI	16,990,675	1.5	N/A	53.0	N/A	N/A	0.48
GSMS 2013-GC14	Indiana Mall	Indiana	PA	14,874,028	1.3	13.1	86.0	72.9	2/1/2020	1.00
CSAIL 2015-C1	Grand River Plaza	Genoa Township	MI	10,022,991	0.8	33.0	100.0	67.0	1/31/2018	1.41
CMLT 2008-LS1	Viking Plaza	Alexandria	MN	9,847,626	3.9	34.1	98.0	63.9	1/31/2019	1.74
COMM 2013-CR7	Sunset Plaza	Norfolk	NE	8,258,275	1.1	33.3	86.0	52.7	1/31/2020	1.67
MLMT 2008-C1	200 - 202 Limestone Road	Frankfort	KY	4,871,070	2.1	62.2	87.0	24.8	1/31/2020	1.18
GSMS 2013-GC10	Schaumburg (Solomon Chicago Portfolio)	Schaumburg	IL	2,887,176	0.4	23.0	89.0	66.0	1/31/2019	2.58

*Bon-Ton is a noncollateral tenant

N/A: Not applicable

Source: Morningstar Credit Ratings, LLC

Occupancy risk is also a concern, as Bon-Ton occupies over 20% of the gross leasable area at 27 properties and 100% of the GLA at 10 of these locations. In total, the occupancy at 42 properties, backing CMBS loans with a combined balance of $1.41 billion, would fall below 80% if Bon-Ton were to vacate. In addition, even loans in which Bon-Ton occupies a smaller part of the GLA could face refinancing issues if they lose the tenant, as the vacant space could indicate problems to lenders. We identified 16 loans, with a property balance of $796.7 million, that are set to mature by the end of 2020.

Loans of Interest

The largest asset of concern is the University Mall in LBCMT 2007-C3, which has been real estate owned since October 2016. The loan’s unfavorable metrics at underwriting, with a debt service coverage ratio of 1.14x and 6.6% debt yield, left it unable to withstand tenant turnover and declining rents. Further, the property’s location in a secondary market and lack of investment from its owner made it difficult to compete with newer properties nearby. A July 2017 appraisal suggests a $44.8 million value, which would lead to a $57.6 million loss based on exposure of $97.9 million and a 10% haircut for liquidation expenses. While Bon-Ton, which occupies 9.8% of the more than 600,000-square-foot property in South Burlington, Vermont, will vacate in January 2018, Target will take over the vacant space in October 2018, according to an article in the Burlington Free Press. Consequently, we believe the loss of Bon-Ton will have little effect on the property's value.

At the Southridge Mall in suburban Milwaukee, the Boston Store isn't part of the collateral, but its loss would be another blow for the property, which will be down two anchor stores by year-end 2018. Noncollateral tenant Sears vacated in September and collateral tenant Kohl's is expected to close by the end of next year. The largest anchor, Boston Store occupies 103,837 square feet of the regional mall. Our $104.0 million value, down 42.5% from the original $181.0 million appraised value, suggests a value deficiency of more than $15.0 million on the $71.8 million loan. The closure of the Boston Store would further erode the property's value, particularly as co-tenancy clauses, which may permit in-line tenants to pay reduced rent or terminate their leases when multiple anchor spaces remain vacant beyond a specified period of time, come into play. The combined loan balance of the two pari passu notes, 7.2% of JPMBB 2013-C14 and 4.1% of JPMBB 2013-C12, stands at $119.6 million. While the Boston Store is collateral for two other pari passu loans in BACM 2015-UBS7 and MSC 2015-UBS8, the tenant's long-term lease that runs until 2035 renders the loan a low risk.

If the Bon-Ton at the McKinley Mall in COMM 2014-CR14 and COMM 2014-LC15 were to vacate, it would be the second anchor to close at the Buffalo, New York, regional mall since 2016. Macy's and Macy's Home Store, both noncollateral tenants, closed in 2016, and the building and land were sold to a developer. Bon-Ton occupies 13.4% of the 724,133 square feet that serve as collateral, with a lease that expires in 2021. While cash flow has been relatively stable since issuance, the loss of a second anchor tenant would have a negative effect on foot traffic and revenue and increases the likelihood of additional co-tenancy clauses being invoked; Old Navy is already paying reduced rent because of Macy's departure. The combined loan balance of the two pari passu notes stands at $35.8 million.

The Susquehanna Valley Mall loan in COMM 2012-LC4 has a high risk of default, as the collateral experienced a drop in cash flow after the loss of two anchor tenants. Sears closed its store earlier this year, and JCPenney shuttered its store two years earlier. The departure of the anchors led to in-line tenants vacating, which pushed the 2016 net cash flow more than 30% below underwritten as December 2016 occupancy fell to 80.0% from 94.7% at underwriting. Bon-Ton, the second-largest tenant, occupies 14.3% of the 628,063-square-foot regional mall about 35 miles north of Harrisburg, Pennsylvania. We value the property at $16.1 million based on a 12% capitalization rate and $2.7 million in net cash flow. The loan balance stands at $25.9 million. The closure of Bon-Ton would further erode the property's value.

Separately, the $80.0 million Chicago Ridge Mall loan, 7.1% of COMM 2012-CR2, does not appear to be a high risk as the property's cash flow would likely absorb the loss of the Carson Pirie Scott store. While the possible loss of the retailer would drop occupancy to 70.9% from 98.0% as of June, our analysis suggests low default risk and an adequate loan-to-value ratio of 51.2%. The collateral, 568,915 square feet of an 867,955-square-foot super-regional mall about 15 miles south of Chicago, has outperformed underwritten expectations with strong occupancy and net cash flow rising more than 20% since underwriting. The cash flow can be attributed to the property's mix of traditional mall tenants and those found in community and power centers, and its densely developed in-fill location limits potential new competition. The property has posted a 3.34x DSCR as of year-end 2016, compared with 2.74x at issuance, while the debt yield was 15.6%.

Overstored and Underinvested

Bon-Ton reported same-store sales declined 6.6% for the quarter ended Oct. 28, its 10th-consective quarterly decline. We expect the retailer to announce more closures as a lack of cash flow hampers its ability to invest in itself and strengthen its brand and customer experience. Our concerns include the lack of a sustainable competitive advantage and growing competition from fast fashion retailers like Zara and H&M, as well as the growth of off-price competition from discount retailers like TJ Maxx and Ross Stores.

Loan-level details for all CMBS loans with Bon-Ton as one of the five largest collateral tenants can be found in Excel format by clicking the download icon at the top of page one.

As we will be monitoring these loans very closely, please see our DealView® CMBS Monitoring Analyses reports in the coming months where property-level analysis, performance, and value analysis will be available at the loan and deal level.

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