CMBS Research

Morningstar Monthly Highlights

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Morningstar Credit Ratings
January 2019 Remittance

Contents

Executive Summary

- The delinquency rate continued its downward trend, improving 2 basis points to 1.69% from 1.71% in December.
- The delinquency rate fell in 10 of the past 13 months and is down 74 basis points from a year ago. Given the ongoing liquidations of legacy loans and steady new origination volume, Morningstar Credit Ratings, LLC believes the delinquency rate will hold below 2.0% well into this year. Longer-term, we expect the delinquency rate to gradually increase as postcrisis deals season.
- The volume of Morningstar Watchlist loans has remained relatively steady the past five months, trickling down by $176.7 million last month to $23.73 billion. While steady or improving property fundamentals should keep the Watchlist balance below its recent peak of $25.23 billion reached in July, a slowing economy and overbuilding in some markets may push the Watchlist balance higher.
- The special-servicing unpaid principal balance improved to a new postcrisis low of $16.95 billion, down $954.1 million from December, and the percentage of loans in special servicing fell 12 basis points to 1.99%.
- Our projected losses on specially serviced loans ticked up to $12.19 billion, an increase of $93.2 million from December, and has remained relatively flat over the past 12 months, down $242.8 million since January 2018.
- The payoff rate of maturing loans in CMBS started the year strong at 96.7%, although we expect it to finish the year at roughly 80% based on 25.4% of loans have LTVs greater than 80%.

Table 1 – Significant Value Changes Among Large Loans

Deal ID	Asset Name	Loan Balance ($)	Value Change ($)	Loss Forecast ($)	Previous MORN LTV (%)	Current MORN LTV (%)
JPMBB 2015-C29, JPMBB 2015-C30	One City Centre	100,000,000	(23,956,415)	12,209,576	133.1	195.5
BSCMS 2007-T28	Charleston Town Center	91,575,936	(23,059,750)	46,576,748	134.6	203.5
GSMS 2014-GC20	Three WestLake Park	80,000,000	(15,800,000)	34,597,039	130.0	175.0
MSC 2011-C2	Towne West Square Mall	45,199,077	(13,200,000)	29,362,083	155.3	284.3
WFCM 2015-C28	3 Beaver Valley Road	44,957,427	(17,107,000)	-	68.6	92.9
COMM 2013-CR13	Park Plaza	17,689,053	(6,000,000)	-	74.6	99.9
WBCMT 2007-C30	Silver Oak - Medical Office Building	15,387,938	(4,084,956)	4,712,894	104.3	144.1
MLCFC 2007-7	Gristmill Village	12,591,266	(3,895,000)	4,897,137	98.0	140.6
COMM 2013-CR8	11000 Equity Drive	10,765,945	10,564,693	-	223.8	70.0
WFRBS 2014-C19	Holiday Inn Express & Suites - LaPlace	10,206,229	(6,900,000)	90,623	63.0	109.7

Source: Morningstar Credit Ratings, LLC

Significant Value Changes Among Watchlist and Specially Serviced Loans

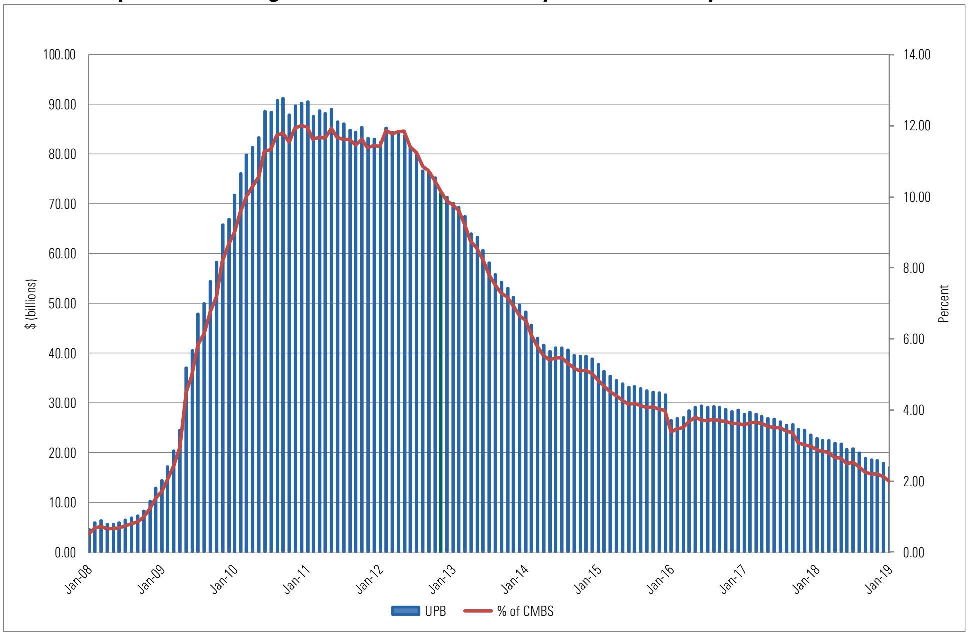
In January, we raised our value on properties securing 12 loans with a combined balance of $156.7 million, while we lowered our values on properties securing 29 loans with a combined balance of $1.07 billion. Of these, 20 loans showed value declines that resulted in increased loss forecasts. For example, we reduced our value of the collateral backing the Charleston Town Center loan to $30.6 million from $68.1 million. The asset, 363,140 square feet of a 931,333-square-foot regional mall in Charleston, West Virginia, backing the $91.6 million loan in BSCMS 2007-T28, became real estate owned in January. The loan initially transferred to special servicing in 2017 after failing to pay off at maturity. Noncollateral Macy's, one of two remaining anchors, announced in early 2019 that it will close, which follows noncollateral Sears' 2017 departure. Morningstar valued the asset at $30.6 million using a 10-year discounted cash flow approach.

Separately, the collateral behind the $80.0 million Three Westlake Park loan in October 2018 was transferred to the special servicer because the largest tenant is vacating, which will leave the Houston office property nearly vacant. At issuance, the nearly 420,000-square-foot office property was 100% occupied by five tenants, although the bulk of the occupancy was attributable to two tenants, ConocoPhillips and BP Corporation North America. BP has since vacated after its lease expired, and ConocoPhillips has been trying to sublease its space under a lease that expires this month. Our discounted cash flow analysis values the property at $45.7 million, which suggests a loss about of $34.6 million.

Special-Servicing Exposure

The special-servicing unpaid principal balance continued its descent, hitting another postcrisis low of $16.95 billion, dropping $954.1 million from December and down $5.95 billion over the past 12 months. The special-servicing rate also hit a postcrisis low of 1.99%, down 12 basis points from December. While legacy CMBS now accounts for less than 3.0% of the CMBS universe, specially serviced loans from deals issued before 2010 represent 70.6% of all specially serviced loans by balance. Retail and office assets continue to represent the bulk of specially serviced loans, with a combined exposure of more than 75%.

Chart 1 – Special-Servicing Balance and Rate January 2008 – January 2019



Source: Morningstar Credit Ratings, LLC

Special-servicing transfers declined by $510.6 million to $436.9 million in January, the largest of which was the $222.6 million MSKP Retail Portfolio - A loan in MLCFC 2007-6. The 2012 loan modification extended the maturity until March 2019 and created a $93.1 million hope note. While the loan re-transferred to the special servicer in January, the collateral is expected to be sold in March, according to servicer commentary. The eight community shopping centers in Florida that secure the loan had an average occupancy of 84.7% and a debt service coverage ratio of 1.51x for the nine months ended September 2018. We forecast a loss on the entire $92.9 million hope note.

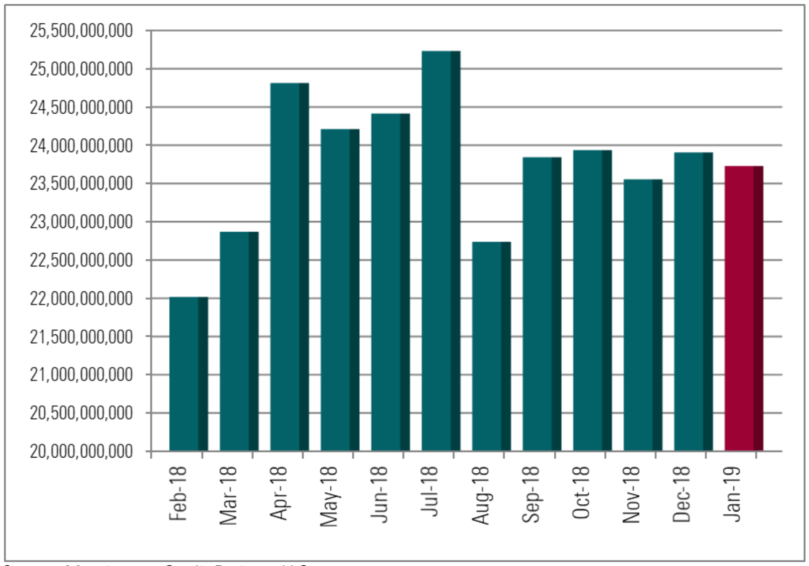
Separately, we do not project a loss on the $50.2 million Heron Lakes loan in JPMBB 2014-C26, which was the largest postcrisis transfer. The loan, backed by seven office buildings totaling 314,504 square feet in Houston, transferred to special servicing because the borrower filed for bankruptcy protection and secured an unauthorized second mortgage. Performance has also deteriorated with June 2018 occupancy sliding to 83.0% from 98.0% at underwriting after the largest tenant departed, which led to a more than 10% decline in net cash flow. Further, with submarket vacancy hovering around 25%, we expect difficulties leasing up vacant space. Lease rollover remains a concern as well because the leases for the remaining tenants expire before the loan matures in 2024. While we do not project a loss, our $51.4 million value suggests a borderline line 97.7% loan-to-value ratio.

Watchlist Exposure

The Morningstar Watchlist volume decreased $176.7 million to $23.73 billion. In January, we added 34 loans with a total UPB of $1.01 billion to the Watchlist, up from $673.2 million added in December. Morningstar also removed 43 loans from the Watchlist, eight of which were transferred to special servicing, while 16 loans paid off.

Although Morningstar's Watchlist balance dropped from its recent peak of $25.23 billion in July, it has increased significantly since reaching a postcrisis low of $17.34 billion in November 2017 suggests that forward-looking risk is increasing. We believe that postcrisis deals will become more exposed to credit events, such as competition from new construction, vacating tenants, and general changes in market demand, as they season. With issuance volumes surging in 2014 and 2015, a large percentage of postcrisis deals are progressing further along the seasonality curve, exposing loans to risks that were not prevalent at issuance, including new supply/increased competition and changing space requirements spurred by technology disruptors across all major property types.

Chart 2 – Morningstar Watchlist Volume – Trailing 12 Months ($)



Source: Morningstar Credit Ratings, LLC

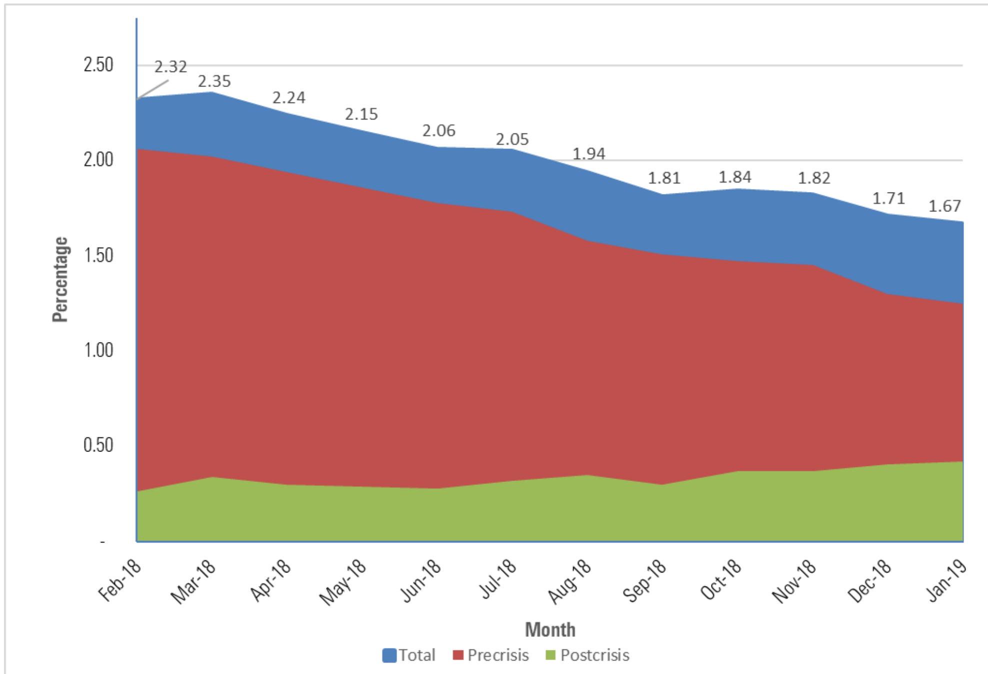
The collateral for the Woodbridge Center loan with pari passu pieces in WFCM 2014-LC16 and WFRBS 2014-C20, the largest master-serviced loan added to our Watchlist at $243.5 million, is 1.1 million square feet of a 1.7-million-square-foot regional mall about 30 miles south of New York City in Woodbridge, New Jersey. Revenue has gradually declined since issuance and is now about 8% lower than underwriting. While near-term default risk is low given the solid DSCR, a continued slide in revenue through the remainder of the loan term creates elevated balloon risk for the April 2024 maturity. Further, we have long-term concerns about the viability of the noncollateral department stores and their impact on the mall's overall desirability moving forward. Adding further stress are the amount of competing supply in the area and the property’s exposure to JCPenney and Sears, which are struggling. The property includes a variety of national and regional credit-rated retailers, the majority of which are committed to long-term leases. In addition to the department stores, the other anchors that are part of the collateral include Boscov's and Dick's Sporting Goods, while Dave & Busters opened in 2017. While the property is in a densely populated area in Northern New Jersey with significant demand drivers, the mall competes with several nearby super-regional malls including Menlo Park Mall (two miles away), The Outlet Collection Jersey Gardens (15 miles) and Bridgewater Commons (20 miles). Our $239.8 million value suggests a 101.4% LTV.

Delinquency

The CMBS delinquency rate continued its decline in January, dipping 2 basis points to 1.69% from 1.71% in December. The balance of delinquent loans stands at $14.36 billion, down $131.3 million from December, and down $4.96 billion, or 25.7%, from the year-earlier period. Delinquencies from deals issued from 2010 through 2018 remain a small portion of the total, representing just 0.42% of the CMBS universe, while delinquent precrisis loans account for 1.25%, suggesting that continued loan workouts and resolutions of precrisis loans will put downward pressure on the overall delinquency rate.

Since peaking at 8.5% in May 2012, the delinquency rate has steadily declined; however, we believe the rate will reach an inflection point in 2019 or 2020. The burning off of legacy loans has been a significant factor in the steady decline in recent years, though its impact will fizzle, with the legacy balance representing less than 4% of the universe today and declining rapidly.

Chart 3 – Monthly CMBS Delinquency by Percentage



Source: Morningstar Credit Ratings, LLC

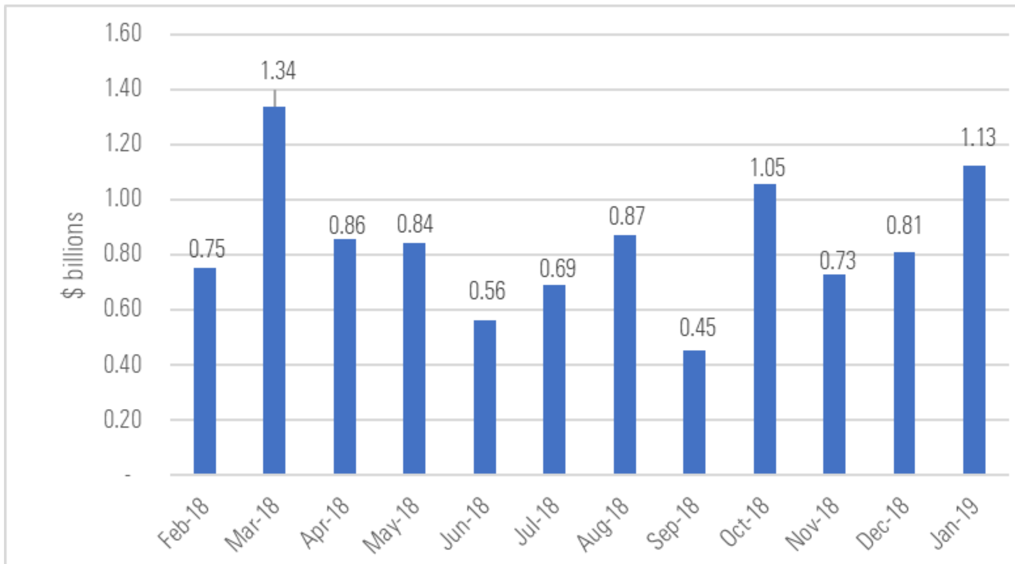
Table 2 – Trailing 12-Month Delinquency ($ UPB in billions)

Category	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19
30-Day	0.86	1.27	1.08	0.79	0.67	1.00	1.10	0.54	0.60	0.72	0.94	1.25
60-Day	0.27	0.34	0.62	0.24	0.26	0.30	0.37	0.23	0.31	0.26	0.39	0.38
90-Day	2.57	2.52	2.26	2.25	2.05	1.65	1.79	1.8	1.7	1.7	1.47	1.72
Foreclosure	5.03	4.85	4.55	4.21	4.24	3.89	3.67	3.43	3.15	2.86	2.62	2.42
Real Estate Owned	9.65	9.86	9.86	10.2	9.83	10.05	9.25	9.07	9.79	9.75	9.07	8.59
Total CMBS Del.	18.38	18.85	18.36	17.69	17.05	16.88	16.19	15.08	15.55	15.29	14.49	14.36
Current	774.84	781.77	800.45	804.38	809.30	807.17	818.93	818.27	828.40	825.05	834.09	836.63
Total CMBS	793.22	800.62	818.82	822.07	826.35	824.05	835.12	833.35	843.95	840.35	848.58	850.99
Delinquency %	2.32	2.35	2.24	2.15	2.06	2.05	1.94	1.81	1.84	1.82	1.71	1.69

Source: Morningstar Credit Ratings, LLC

The volume of newly delinquent loans rose $318.4 million to $1.13 billion in January and is above the 12-month moving average of $839.4 million. The previously mentioned $50.2 million Heron Lakes loan in JPMBB 2014-C26 was the largest newly delinquent loan that remains delinquent as of this report date. Separately, the $46.4 million One West Fourth Street loan in COMM 2013-CR7 fell delinquent after the borrower chose not to move forward with a discounted payoff. The loan transferred to special servicing in 2016 after the largest tenant, Wells Fargo (46% of gross leasable area), vacated the 431,465-square-foot Winston-Salem, North Carolina, office building. Our $28.9 million value suggests an $18.1 million loss.

Chart 4 – Newly Delinquent Loans



Source: Morningstar Credit Ratings, LLC

Compared with year-ago levels, the office sector saw the largest decline in delinquent balance, tumbling $2.20 billion, or 34.3%, to $4.22 billion as liquidations far outpaced newly delinquent loans. By dollar amount, the other four major property types exhibited the following activity year over year:

- Retail loan delinquency dropped by $1.04 billion, or 14.5%, to $6.10 billion from $7.14 billion one year ago, because more loans were either liquidated or resolved than were replaced with newly delinquent loans.
- Industrial loan delinquency had the largest percentage decrease, falling 61.3% to $358.0 million from $924.7 million one year ago.
- Multifamily loan delinquency rose by $131.6 million, or 9.7%, to $1.49 billion from $1.36 billion one year ago.
- Hotel delinquency declined by $1.04 billion, or 48.3%, to $1.12 billion from $2.16 billion one year ago because of several large loans that were liquidated or paid off.

Table 3 – January Delinquency by Property Type

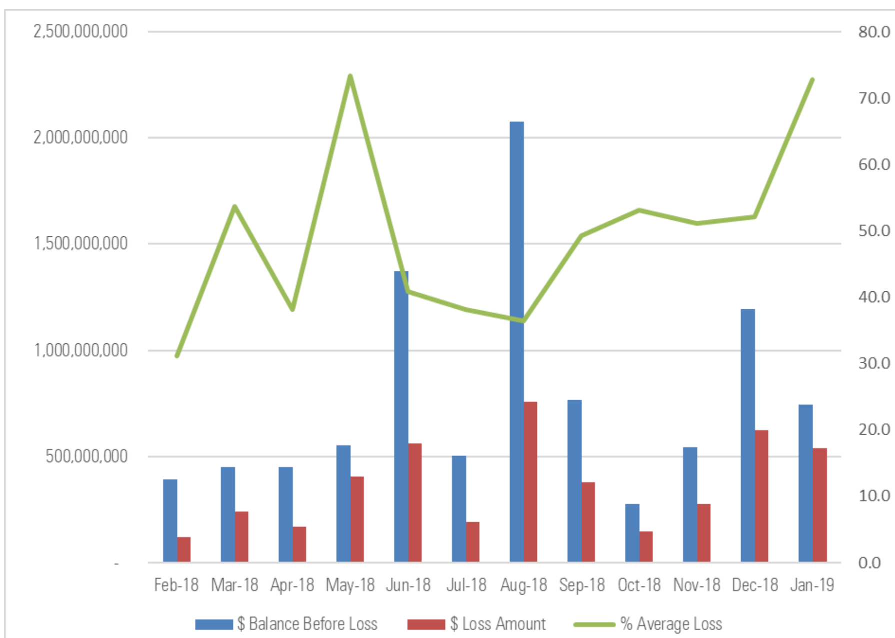
Property Type	$ Current Balance	# Loans	% of CMBS Universe	% of CMBS Delinq.	% of Property Type
Healthcare	59,630,000	3	0.01	0.42	2.73
Hotel	1,116,843,780	81	0.13	7.78	1.42
Industrial	358,003,317	26	0.04	2.49	1.51
Multifamily	1,490,249,234	391	0.18	10.38	0.34
Office	4,216,666,478	186	0.50	29.36	3.36
Other	1,018,701,868	47	0.12	7.09	1.55
Retail	6,100,078,941	413	0.72	42.48	4.84
Total	14,360,173,618	1,147	1.69	100.00	-

Note: Figures may not sum to totals because they are rounded.
Source: Morningstar Credit Ratings, LLC

CMBS Liquidations

The weighted-average loss severity in January swelled to 72.8%, the second-highest level since we began tracking the statistic in 2005. About $743.1 million in debt was written off, down from $1.20 billion in December, with precrisis loans representing nearly 90% of the liquidated balance. The full loss on the $50.0 million City Place B note was the largest write-off. The loan backed by the West Palm Beach mixed-use complex consisting of residential, retail, and office space was modified in 2012, which split the note into an A and B component. Sagging performance spurred the loan's second transfer to special servicing in 2016.

Chart 5 - Trailing 12-Month CMBS Liquidations and Losses

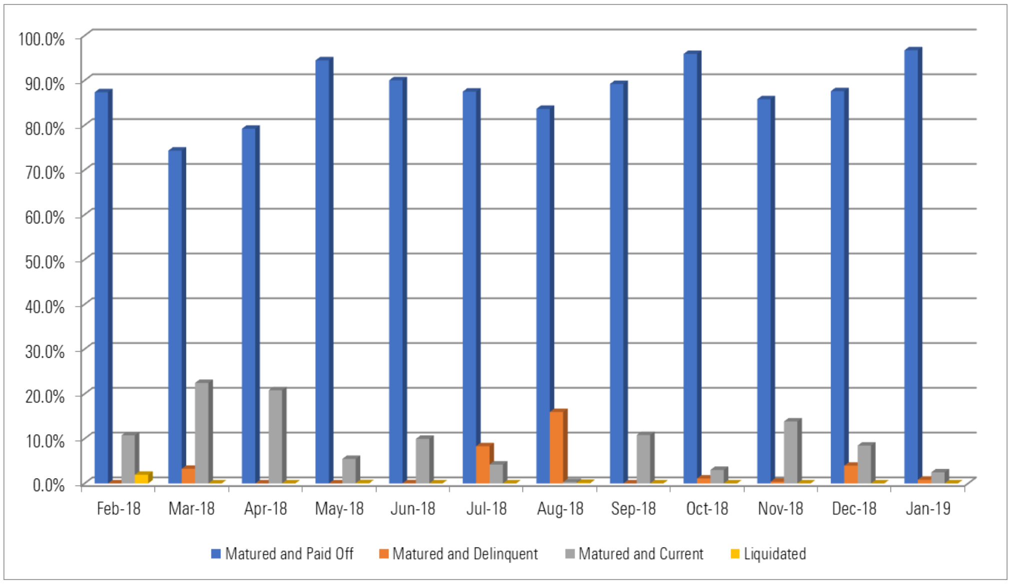


Source: Morningstar Credit Ratings, LLC

Monthly Maturity

After finishing 2018 with an 84.3% maturity rate, 2019 got off to a strong start as 96.7% of maturing loans successfully paid off. The $16.0 million Hilton Garden Inn Pittsburgh – Cranberry in GSMS 2014-GC18 is the largest loan that failed to pay off and remains outstanding as of the date of this report. The property has seen a significant decline in net cash flow, down more than 40% since underwriting, and the September 2018 debt service coverage ratio tumbled to 1.10x from 1.78x at issuance. The collateral, a 136-unit limited-service hotel built in 2012, about 20 miles north of Pittsburgh, was 68.0% occupied in September, down from 74.7% at underwriting. As we first warned readers in our July 2018 Alert, What's the 411 on 412 Area Hotels?, we remain concerned that Pittsburgh's burgeoning hotel-room supply has increased risk on more than $250 million in commercial mortgage-backed securities.

Chart 6 – 12-Month Performance Trend by Loan Status at Maturity

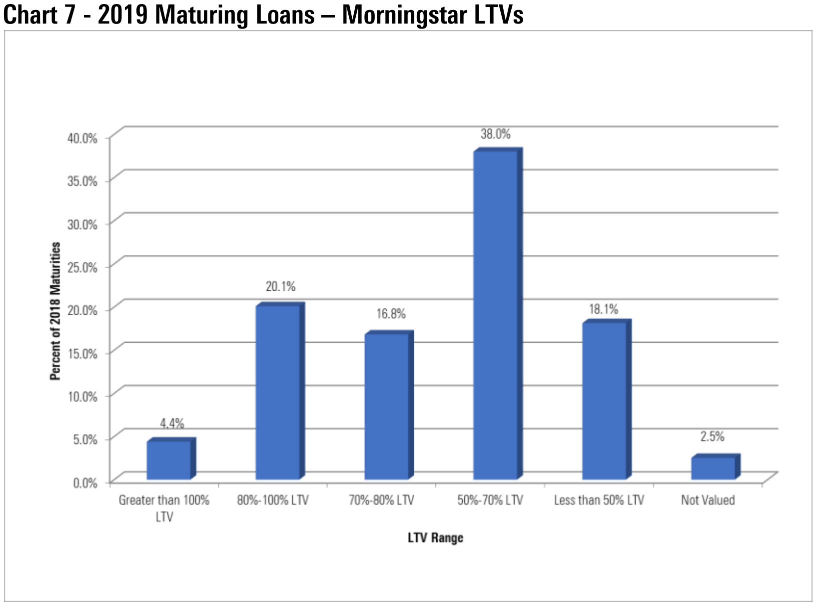


Source: Morningstar Credit Ratings, LLC

Maturity Outlook for 2019

Looking ahead to 2019, some $10.17 billion of CMBS loans will mature. We have valued approximately 95.6% of them and project that the on-time payoff rate will come in at roughly 80%, based on the fact that 25.4% of loans have LTVs greater than 80%. This information is displayed in Chart 7.

Chart 7 - 2019 Maturing Loans – Morningstar LTVs



Source: Morningstar Credit Ratings, LLC

Although LTV is a reasonable barometer in Morningstar's maturity analysis, a loan's refinancing ability is also subject to its debt service coverage ratio, debt yield, amortization, and lease expiration risk. Beyond an individual property's performance, factors such as capitalization rates and specific real estate market trends also will influence a loan's refinance prospects.

Once logged into Morningstar's CMBS Credit Risk Monitoring and Analytics, clients have access to loan-level details for all maturing loans in Microsoft Excel format by clicking the download icon at the top of Page 1.

Detailed Morningstar analyses and value estimates for all delinquent, matured-delinquent, and matured-current loans as well as loans on the Morningstar Watchlist can be found in the respective Morningstar DealView CMBS Monitoring Analyses or Watchlists.

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