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News & Information

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CRE Capital Markets Outlook "Cloudy," Experts Confirm

For the past year, most of us working in CRE have been watching closely as capital markets respond to an increasingly difficult set of challenges.

Over that period, we've seen the cost of debt skyrocket, while the increasing threat of a wave of loan delinquencies and collapsing transactions has made for one of the most precarious debt environments we've seen in a long time.

The question that's hung in the balance all the while has been: should we be preparing for things to get worse?

Stormy Weather Incoming

According to a recent Commercial Observer (CO) article, the answer is a firm "yes." Reporting on the June Research Bulletin by Yardi Matrix analysts, CO notes that analysts' "worst fears" have been confirmed by a combination of plunging transaction activity, rising debt costs and rising commercial mortgage-backed securities (CMBS) delinquencies.

Yardi's report comes on the back of the recent Commercial Real Estate Finance Council (CREFC) annual conference, which took place in New York in June.

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Rising Delinquency, Low Demand

Drawing on the opinions of panelists at the CREFC event, as well as additional data from industry analysts, Yardi notes several concerning trends and weak points in the current CRE finance landscape. Among those trends are:

- Commercial asset values have decreased by 15% compared to March 2022 with office (-27%) and apartment (-21%) assets noted as the worst performers,
- Around 7.3% of loans that matured in Q1 are delinquent,
- Nearly 19% of loans that matured in April/May are delinquent, and
- CMBS volume has declined 74% year-over-year.

Unsurprisingly, these developments have investors worried. Yardi Director of Research, Paul Fiorilla, comments: "There's so much uncertainty in the CRE market right now — about the direction of interest rates and pricing, and the performance of properties — that investors have heightened concerns about the potential problems of repaying loans."

Fiorilla adds that as a result, many investors are very wary of bonds backed by commercial mortgages in the current market, especially when it comes to those backed by office and hospitality assets.

Calculated Defaults

One of the more surprising findings from the Yardi Bulletin is just how many borrowers are deliberately defaulting on properties they no longer want. Many of these borrowers are large, well-capitalized firms that have the funds available to avoid defaulting when problems arise.

These moves add an additional layer of complexity to the already challenging debt environment. Yardi notes that lenders are viewing the development as a "dangerous game" being played by large firms which typically get better loan terms because their risk of default has historically been lower.

Quoted in CO, Fiorilla adds: "It's obviously a strategic thing that has caught lenders by surprise."

Keeping Informed

In the current challenging environment, one of the best ways CRE professionals can prepare for what's to come is to stay up to date on the latest developments. For our part here at NAI, we'll be keeping a sharp eye on CRE capital markets and reporting back as the situation develops.

In the meantime, we recommend taking a look at the full Yardi repor, and keeping an eye on the NAI Global "News and Insights" page for the latest information on what's happening in the world of CRE.