List of Office Loan Defaults "Growing" as Economic Uncertainty Deepens

According to a recent article in CoStar News, commercial real estate (CRE) investors Columbia Property Trust have defaulted on a $1.72 billion loan, leaving it 30 days delinquent.

The news comes hot on the heels of several other loan defaults, including Brookfield's $784 million loan for two office towers in downtown Los Angeles, and Blackstone's office troubles in Europe.

Growing concerns

Quoted in the CoStar article, credit-rating firm DBRS Morningstar stated: "Some 20.8% of a $65.5 billion outstanding loan balance that's backed by office properties in New York, Chicago, and San Francisco, the three most concentrated office markets in the United States, have a rollover risk through the end of 2024."

DBRS further noted that they expect older Class B and C office buildings to "take the first hit," but that eventually even Class A properties could be affected.

National Perspective

In a speech given to the Institute of International Bankers, Federal Deposit Insurance Corporation (FDIC) Chairman, Martin Gruenberg, echoed this cautious outlook on office.

Gruenberg started by noting that, in general, US CRE loans at banks "grew 10.7 percent during 2022", and that lending for construction and new development went up 16.5%. He added that most commercial property types "performed well in 2022," but that the case for office was far less clear.

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Citing data from CoStar and Trepp, Gruenberg pointed out that office vacancy has consistently "trended up" nationally over the past several years, from 9.6% in March 2020 to 12.5% at year-end 2022, lowering operating incomes on the property class.

Delinquency Rising

The combination of lower operating income and higher interest rates (which make it more expensive to refinance loans when they come due) could drop the valuations of office properties over time.

Gruenberg added: "Some of the loans financing these properties are whole loans held on the balance sheets of banks, some are syndicated and sold, and many serve as collateral for CMBS [commercial mortgage-backed securities]. There are early indications that delinquencies on office property in CMBS are starting to tick up."

He noted that there was some good news in that default rates "remain low at this time," but that the situation was an area of "ongoing supervisory attention."

Office (and Others)

While it can't exactly be considered 'good news,' it should be noted that office isn't the sole asset class facing defaults and declines in the tumultuous environment of early 2023. The multifamily sector, which has shown outsized performance throughout the pandemic, has also started showing signs of loan stress and even the industrial sector's years' long run is slowing.

Whether these are the early signs of a larger trend of accelerating delinquency and default rates remains to be seen. As always, we'll be keeping an eye on things, and updating our outlook, as the situation develops.