CUSHMAN & WAKEFIELD
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DEBT MARKET TALKING POINTS – 3/11/2024

Economy and Financial Markets

- Market sentiment for a "soft landing" is still the consensus, but hot Q1 macroeconomic and inflation data has presented upside risks, challenged the deceleration narrative, and forced investors to recalibrate expectations for the timing and depth of a Fed pivot.
- Last year the U.S. economy grew 2.5% based on the second estimate of Q4 GDP that showed the growth at an annualized rate of 3.2% in the last quarter of 2023, down from 4.9% in Q3.
- The February jobs report contained mixed signals interpreted to support the soft-landing narrative with a strong headline of 275,000 jobs added (beating estimates of 198,000), but also the unemployment rate ticked up to 3.9% and wage growth slowed to 0.1%, "cooler" than forecast. Additionally, the red-hot January report was revised down from 353,000, to a smoother 229,000.
- January retail sales dropped 0.8% from the prior month (up 0.6% YoY), down from a 0.4% gain in December and the largest decline in 10 months. A post-holiday pullback in the January report is normal, but this was more than double the decline anticipated by economists.
- January inflation data came in hot suggesting the risk of potential reacceleration. Headline CPI rose 0.3% from the prior month (3.1% YoY), and core CPI (ex-food and energy) rose 0.4% (3.9% YoY). This is the second month in a row inflation exceeded expectations. Core PCE, the Fed's preferred inflation index, increased 0.4% from the prior month (2.8% YoY), the fastest monthly increase in a year. February CPI data is due out March 12th.
- As expected, the FOMC held the target range at 5.25-5.50% at the January meeting and indicated the need for patience and more confidence that inflation is sustainably moving to 2% before the first cut, thereby taking the possibility of a March rate cut off the table. January's accelerating inflation data caused the market to unwind expectations for rate cuts this year. As of this writing, the market expects the first rate cut in June, and a total of approximately three to four cuts in the calendar year.
- Yields have been fluctuating as traders have re-accepted the higher-for-longer outlook, driven by mixed macro data that suggests upside risks for economic reacceleration.
    - *Fixed:* The 10Y UST yield is currently around 4.10%, down ±90 bps from the peak in October, and down ±25 bps from Q1's recent highs. Treasury yields remain susceptible to volatility induced by macro data and Fed speak.
    - *Floating:* Consensus is that the peak is here, but the notable change in recent weeks is that the market has re-adjusted the outlook for rate cuts from five or six in 2024 (125-150 bps), down to three to four (75-100 bps), closer to the FOMC's forecast of three cuts.

INDEX SUMMARY				
(Rounded)		Change		
	3/11/2024	1 WK	1 MTH	YTD
SOFR				
30-Day Average	5.30%	0 bps	0 bps	-5 bps
1-month Term SOFR	5.30%	0 bps	0 bps	-5 bps
Treasury				
5 Year	4.10%	-10 bps	-5 bps	25 bps
7 Year	4.10%	-15 bps	-5 bps	25 bps
10 Year	4.10%	-10 bps	-10 bps	25 bps
SOFR Swap				
5 Year	3.85%	-10 bps	-5 bps	30 bps
7 Year	3.75%	-15 bps	-10 bps	25 bps
10 Year	3.70%	-15 bps	-10 bps	20 bps

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CRE Debt Themes

- Investor / lender sentiment is hopeful but cautious that 2024 marks "the bottom" and the start of a recovery for the CRE market. Focus has shifted from interest rate risk to CRE fundamentals risk, with a renewed focus on operations and cash flow durability. There's optimism for the path forward in anticipation of rate cuts and an economy that can either soft-land or only experience a mild recession. Consensus is that interest rates have peaked, although the timing and pace of cuts is still uncertain. An easing rates regime should help CRE cap rates stabilize which will help thaw debt and equity capital and deploy dry power sitting on the sidelines.
- Q1 CRE transaction volume has been slower than expected but is picking up. The "everything rally" at the end of last year sent interest rates lower and seemingly added to the bid-ask spread between buyers and sellers, as sellers weighed whether to sell and at what price, holding out hope that lower rates and a pending Fed pivot could boost values, while buyers shifted focus away from interest rates to CRE fundamentals and uncertainty around operations / NOI. The recent unwinding of expectations for rate cuts has helped owners refocus and make decisions to sell or refinance. Overall, the expectation is 2024 will be a more active year for CRE transactions, but the slow start to Q1 combined with uncertainty surrounding the upcoming U.S. presidential election in Q4, compresses the viable window. Our advice to most clients is to go to market now if you need to transact this year.
- Interest rates are still elevated but greatly improved since Q4. Fixed rate loans are benefitting from Treasury yields that are ±90 bps lower than the October peak (5.00% to 4.10%) but remain volatile to macro data and Fed speak. Corporate bond spreads are near post-GFC tights, pricing in the strength of the economy and anticipating a soft landing, which has helped CRE mortgage spreads tighten in sympathy. CRE spreads could narrow more if Treasury yields remain low and it becomes clear that the economy will enjoy a soft landing. CMBS spreads have improved the most of any lender type. At the top of the stack—AAA bond spreads are ±60-65 bps tighter—to levels we haven't seen in two years. Combined with improvement in lower rated tranches, the net result is that CMBS issuance is up dramatically YTD, as large SASB loans have become viable again.
- Whether to go fixed rate or floating rate depends on the deal profile and investment horizon, but borrower demand for fixed rate has overwhelmingly been for shorter duration with some prepayment flexibility on the back end. Shorter duration 5Y fixed rate loans make sense for borrowers that want out of floating rate loans, but do not want to be locked into higher rates long-term. The rationale being that short term fixed rate debt can carry the property through the next few years of uncertainty while minimizing interest rate risk, eliminating cap costs, and avoiding origination / extension fees. Fixed rate borrowers are also negotiating for more open period, taking advantage of rate buy-downs to improve proceeds, and executing early rate locks.
- Liquidity has improved and there is competitive debt capital available for good assets located in growth markets for top tier sponsors. Lenders are leaning-in to compete for a limited supply of high-quality loan opportunities. Agency, life company, and debt fund lenders continue to be the most active capital sources targeting quality multifamily and industrial but also proven hotels and retail centers, and alternatives such as data center, select life science and medical office, self-storage, and multifamily subtypes like senior housing, student housing, and SFR/BTR. Early signs of activity from banks suggests some loosening of credit. Banks are more frequently issuing competitive quotes, but almost always reserved for strategic clients. CMBS has become a viable solution again for very large loans and / or collateral that can't get financed elsewhere.
- Cap stack stress will lead to more forced capital events in 2024. Lower interest rates are good for CRE, but rates are unlikely to come down far enough, fast enough to avoid distress for transitional loans on overvalued properties, leading to more forced sellers, short sellers, and recapitalizations.

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Life Company

- Life companies are competitive for core profile loans and anxious to deploy 2024 allocations, with origination volume targets same or higher than last year. Corporate bond spreads are hovering around post-GFC tights, which has helped mortgage spreads compress in Q1.
- Borrower demand is still heavily oriented towards 5Y fixed with prepayment flexibility in the last two years, while lenders want duration.
- Pricing for low leverage / high DSCR loans is T+ 150s to 170s (~5.60-5.90%), but in practice many loans are low leverage / low DSCR pricing T+ high-100s to very low-200s (~5.90-6.20%).
- Floating rate is available for core low leverage loans SOFR+ high 100s to mid-200s, 50 bps fee, 3+1+1.

INVESTMENT GRADE CORPORATE SPREADS

		Change			52 Week		
	3/8/2024	1 WK	1 MTH	YTD	Average	High	Low
IG Corp (bps to Treasuries)							
Cash Bond	110	-2 bps	2 bps	-1 bps	134	171	103
7-10 Year Cash Bond	121	-3 bps	-2 bps	-1 bps	149	190	116

Source: J.P. Morgan

Debt Fund / Mortgage REIT

- Debt funds and other nonbank lenders remain active filling the gap left by banks and other lender types. 2023 saw significant fund raising for debt strategies, but faced challenges to deploy due to less transactions, tighter credit standards, and increased competition.
- Spreads have compressed under pressure to deploy capital, improved terms and availability of line leverage / repo, a significant improvement in the CLO market, and a lack of transaction volume that is fueling competition for the best loans.
- Terms vary by profile, but the best pricing is mostly in the SOFR+ high 200s to low 300s:
  - 60-70% LTC: high 200s to mid-300s spreads for preferred asset classes, in the lower half of the range with some in-place cash flow
  - 65-75% LTC: 350-450+ spreads for other asset classes / heavier lift business plan / riskier profile / weaker markets / small balance loans
  - Market SOFR floor is 3.00%

Bank

- Banks are still selective, managing existing CRE exposure and reserve requirements, but there has been a moderation of the sharp tightening in credit conditions in recent months, suggesting some improvement. Banks are more frequently issuing strong quotes, but almost always reserved for key clients. Foreign banks have been a notable bright spot relative to domestic money center and regional banks.
- Floating rate spreads for low leverage stabilized cash flowing deals are generally in the very high 100s to mid-200s over SOFR, and swapped interest rates are generally in high 5's% to mid-6% range. More transitional profiles are mid-200s to 300 over SOFR.

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CMBS

- CMBS has been a bright spot in 2024, with issuance up, spreads down and renewed demand for loans from borrowers. Spreads have tightened dramatically in Q1 as bond buyers recognized the relative value to corporates and gained confidence in the outlook for peak interest rates and optimism for a soft-landing economy. Borrowers have taken advantage of improved interest rates and rushed to execute financings to take advantage of a combination of compelling spreads and lower treasury yields. Issuance is on pace to surpass $15B of conduit and SASB in Q1, almost double the amount in Q1 2023.
- AAA conduit spreads are T+ 95, and AAA SASB spreads for the best profile deals are T+ 140-150s but range widely by asset class / profile. Recent macroeconomic data adds some uncertainty and likely leaves bond spreads trading sideways until there's more clarity.
- Lenders are quoting conduit coupons in the mid 6's% to 7% (5Y T+ 250-325 / 10Y T+ 200-275). Best fixed rate and floating rate SASB spreads are generally 200-225 over depending on asset class and leverage, however deals perceived to be inferior can be much higher.
- Borrowers can "buy-down" the interest rate to maintain proceeds at a cost of 1% of the loan amount in exchange for 24-27 bps off the 5Y spread (14-15 bps off 10Y).

CMBS SPREAD SUMMARY

		Change			52 Week		
	3/8/2024	1 WK	1 MTH	YTD	Average	High	Low
Conduit (bps to Treasuries)							
AAA 3 Year	88	-5 bps	-8 bps	-26 bps	131	160	88
AAA 5 Year	142	-2 bps	-6 bps	-33 bps	172	197	142
AAA 30% 10 Year	92	-2 bps	-5 bps	-33 bps	141	179	92
AAA 20% 10 Year	129	-3 bps	-9 bps	-66 bps	210	268	129
AA-	162	-3 bps	-6 bps	-71 bps	277	393	162
A-	270	-6 bps	-5 bps	-95 bps	437	578	270
BBB-	760	-16 bps	-10 bps	-118 bps	911	998	760

Source: J.P. Morgan

CMBS NEW ISSUANCE

Pricing Date	Deal Name	Size ($MM)	Property	Term	Ext.	AAA	BBB-
Conduit (bps to Treasuries) - Trailing 90 Days							
1/30/2024	BANK5 2024-5YR5*	$519.0	NA	NA	NA	99	NAV
1/29/2024	BBCMS 2024-C24	$694.0	NA	NA	NA	95	670
1/25/2024	BMO 2024-5C3*	$902.0	NA	NA	NA	101	NAV
1/19/2024	BMARK 2024-V5*	$884.8	NA	NA	NA	103	NAV
SASB Floating (bps to SOFR) - Trailing 90 Days							
3/6/2024	BX 2024-XL5	$2,350.0	Industrial	2	1,1,1	145	275
3/1/2024	DK 2024-SPBX	$485.0	Self-Storage	2	1,1,1	150	275
3/1/2024	NRTH 2024-PARK	$650.0	Retail	2	1,1,1	170	NA
2/29/2024	BX 2024-PAT	$293.0	Office	2	1,1,1	215	NA
2/28/2024	GWT 2024-WOLF	$1,000.0	Lodging	2	1,1,1	160	295
2/14/2024	BLP 2024-IND2	$615.0	Industrial	2	1,1,1	140	265
2/7/2024	MCR 2024-HTL	$281.0	Lodging	2	1,1,1	185	400
2/6/2024	BX 2024-MF	$550.0	Lodging	2	1,1,1	150	275
1/24/2024	BX 2024-BIO	$1,140.0	Medical-Office	2	1,1,1	170	370
1/17/2024	BX 2024-XL4	$1,500.0	Industrial	2	1,1,1	150	320
SASB Fixed (bps to Treasuries) - Trailing 90 Days							
3/1/2024	WB 2024-HQ	$475.0	Office	4	NA	200	NA
2/7/2024	GSMS 2024-70P	$395.0	Lodging/Retail	5	NA	169	374

**5-Year AAA*

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Agency

- Agencies remain focused on mission-driven business but can still be competitive for best-in-class non-mission loans. FHFA's 2024 multifamily loan purchase cap is $70B for each enterprise with a 50% mission-driven minimum percentage. The caps are down ~$5B each from the prior year but should be more than adequate for anticipated transaction volume.
- Hyper focused on sponsorship / relationships and being selective for which deals and markets to lean-in on with a focus on top line revenue trends and expense assumptions.
- Fannie Mae and Freddie Mac both have appetite to utilize their pre-stabilization loans for new construction lease-up deals that are 65%+ occupied, 75%+ occupied at close with strong leasing velocity and clear path to stabilization within three to six months after closing.
- Fixed rate spreads generally range from T+ 150-170s for mission and T+ 160-180s for non-mission (mid 5's% to 6% coupon), depending on sponsorship and deal profile.
- Borrower demand is for shorter duration 5Y term, and many are taking advantage of the ability to "buy-down" the interest rate to maintain higher proceeds at a cost of up to 1.25-2% of the loan amount in exchange for 28-38 bps off the 5Y spread (25 bps off 10Y) to achieve a low to mid-5's% interest rate.
- Agencies willing to consider 35-year amortization and pricing discounts for loans where Sponsorship is willing to opt into the Workforce Housing Preservation (Freddie) and Sponsor-Dedicated Workforce (Fannie) programs where at least 20% of units are set aside as affordable at 80% of AMI.

AGENCY SPREAD SUMMARY

		Change			52 Week		
	3/8/2024	1 WK	1 MTH	YTD	Average	High	Low
Agency CMBS (bps to Treasuries)							
10/9.5 DUS TBA	59	-2 bps	-5 bps	-5 bps	77	95	59
Freddie K A1	60	-1 bps	-1 bps	2 bps	68	81	55
Freddie K A2	57	0 bps	-1 bps	0 bps	71	84	56
Freddie K B	216	-10 bps	-12 bps	-47 bps	290	350	216
Freddie K C	314	-12 bps	-14 bps	-49 bps	403	500	314

Source: J.P. Morgan

Construction

- Construction loan liquidity has improved some but is still not deep. Select banks, life companies, and debt funds are lending nonrecourse construction for compelling projects, but the field of competitive A-note lenders is thin. Pricing and terms are heavily dependent on project specifics, including asset class, sponsorship, and loan size.
- The pipeline of construction loan demand from borrowers has waned as investors focus on below-replacement cost acquisition opportunities. Those that are moving forward tend to have a legacy basis and / or are already capitalized and plan to take advantage of the shrinking supply pipeline and hope to deliver into a market with less competitive product, poised to capture demand.
- Multifamily and spec industrial:
  - Non-recourse 45-55% LTC, SOFR+ 325-375
  - Mezz / pref available up to 75-80% LTC at 13-15%, but in practice many loans are executing last dollar 65-70% LTC at low double-digit returns, blending the whole loan spread to SOFR+ mid 400s to low-500s