DEBT MARKET TALKING POINTS

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October 16th, 2024

Economy and Financial Markets

- The Fed kicked off the easing cycle, marking the beginning of the end of the capital markets recession that plagued interest rate sensitive markets for the past 2.5 years. Markets cheered the pivot and priced in a faster pace of rate cuts than Fed guidance indicated, however, a surprising surge in the September jobs report and firm U.S. data, coupled with China-stimulus and risk of rising oil prices on Middle East tension have renewed concerns about a "no landing" scenario where the economy continues to grow and interest rates come down more slowly. C&W's base case still calls for a soft-landing with GDP growth slowing through Q1 of next year, after which it rebounds as rates reach less restrictive and more neutral territory.
- The U.S. economy grew 3.0% in Q2, up from 1.6% in Q1 (revised), primarily driven by a pick-up in consumer spending. Q3 GDP is expected to show another 3%+ growth rate. The advance estimate of Q3 GDP is due out October 30th.
- The September jobs report delivered a surprise 254,000 jobs (beating consensus estimates of 150,000), a sharp increase over August's 159,000 (revised), and the unemployment rate ticked down to 4.1%. The Fed has refocused on the employment-side of its dual mandate so, as more jobs data comes in, either the September report is an outlier subject to revisions, or the Fed will not cut as much as the market expects.
- August retail sales rose 0.1% from the prior month (up 2.1% YoY), marking four consecutive months of gains, evidence that consumers are still willing to spend. September retail sales data is due out October 17th.
- September inflation data came in a little hotter than expected but not enough to change outlook for the path to the Fed's 2% inflation target. September CPI rose 0.2% from the prior month (2.4% YoY), and core CPI (ex-food and energy rose 0.3% (3.3% YoY). August's core PCE, the Fed's preferred inflation index, rose 0.1% from the prior month (2.7% YoY). September core PCE is due out October 31st.
- The FOMC cut 50 bps to 4.75-5.00% at the September meeting and officials' median projection recalibrated to include two more 25 bp rate cuts in 2024, for a total of 100 bps this year, up from just one 25 bp cut projected in the June SEP. Inflation is already in-line with the Fed's year-end forecast and focus has shifted from inflation to the labor market. Fed Chair Powell's message is that the economy is in good shape, and they intend to keep it that way, he doesn't believe the Fed is behind the curve and the 50 bp cut should be interpreted as a sign of their commitment not to get behind.
- After an initial drop in yields triggered by softer economic data leading up to the September FOMC and the magnitude of the first rate cut, yields have reversed higher in recent weeks on resurgent strong economic data.
  - *Fixed:* The 10Y UST yield is currently around 4.00%, after bottoming at 3.63% in mid-September, but still down ±70 bps from the YTD peak at the end of April. Treasury yields remain susceptible to volatility induced by macro data, geopolitical events, and the outcome of the U.S election.
  - *Floating:* The market has recalibrated expectations for the path of Fed Funds to a terminal rate range of 3.25-3.50%, implying an additional 150 bps of easing through YE 2025, down from expectations at the end of September of 200 bps / 2.75-3.00% terminal rate. The market expects a 25 bp cut at the next FOMC meeting on November 7th.

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DEBT MARKET TALKING POINTS

INDEX SUMMARY				
(Rounded)		Change		
	10/16/2024	1 WK	1 MTH	YTD
SOFR				
30-Day Average	4.90%	-45 bps	-45 bps	-45 bps
1-month Term SOFR	4.80%	-30 bps	-30 bps	-55 bps
Treasury				
5 Year	3.85%	-5 bps	45 bps	0 bps
7 Year	3.90%	-10 bps	40 bps	5 bps
10 Year	4.00%	-5 bps	40 bps	15 bps
SOFR Swap				
5 Year	3.50%	-10 bps	40 bps	-5 bps
7 Year	3.50%	-5 bps	40 bps	0 bps
10 Year	3.55%	-5 bps	40 bps	5 bps

CRE Debt Themes

- Lender and investor sentiment is the best it's been since early Q1 2022—there's optimism that the CRE market is turning the corner and the capital markets recession is over. While questions remain around the path for the real economy and CRE fundamentals, concerns of systemic CRE risks have faded, and there's a higher probability for a soft-landing economy. Confidence is growing around asset values/calling the bottom as transaction volume increases. Finally, the cost and availability of CRE debt is the most compelling it's been in 2.5 years.
- CRE debt bottomed this time a year ago and steadily improved throughout 2024. Debt availability continues to improve, spreads are stable/tightening, and base rates are on a downward trend despite Treasury yield volatility. Compared to October 2023, fixed interest rates are -125-150 bps lower and positive leverage is possible for many assets. CRE spreads are stable with room to tighten based on corporate bond spreads and strong demand for CMBS bonds, a leading indicator for broader CRE debt that's essential for a healthy functioning market. Large portfolio SASB financings are competitive and accretive, boosting YTD CMBS issuance to be one of the best years post-GFC. Finally, banks are reemerging competitive and hungry for term debt backed by cash flowing assets, a positive change in momentum after lagging other debt capital sources for years.
- The Fed's September rate cut kicked-off the easing cycle and provided welcomed relief and a reason for optimism. While lower interest rates are not the cure-all for CRE, it lays the foundation for recovery. The market is currently pricing -150 bps more cuts between now and YE 2025, but the pace of cuts will depend on the path of the economy: a stronger economy → slower cuts, a weaker economy → faster cuts. Fixed rate borrowers watching long-term Treasury yields should not assume that when the Fed cuts that Treasury yields will decline because Treasury yields move ahead of the Fed, predicting where Fed Funds will ultimately land. It's unlikely the 10Y Treasury gets down to lower 3's% without the economic outlook deteriorating beyond what's currently expected, and the 10Y Treasury is unlikely to rise materially above 4.00% unless the outlook for the economy improves and the target terminal rate for Fed Funds increases.
- The U.S. election has been a talking point in client meetings all year, but as of this writing there's been little to no disruption of debt capital or active sale processes, however most sellers/brokers have positioned the next wave of sale offerings to launch early 2025. History shows that CRE investors will be active transacting regardless of the presidential election outcome, but a split White House/Congress may be the best outcome for CRE to maintain status quo. A sweep by either party could cause interest rates to climb as the controlling party is more likely to pass one-sided legislation that would add to the fiscal deficit and result in added term premium to Treasury bonds.
- A rebound in transaction activity ahead sets up 2025 and 2026 for a significant jump in volume as the Fed delivers a string of rate cuts and long-term yields stabilize, softening upward pressure on cap rates, and giving equity capital the confidence to deploy for new acquisitions.

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Life Company

- Heading into year-end there is still strong appetite for core profile loans, however, allocation limits have become a constraint for some accounts. The most competitive life companies are still quoting terms as aggressive as earlier in the year, but the depth of those bids has started to wane for loans that need to rate lock or close by year-end.
- Mortgage spreads remain steady in sympathy with corporate bond spreads near post-GFC tights, reflecting a bullish outlook for the economy. Pricing for low leverage / high DSCR loans is 5Y T+ 140s to 160s (~5.25-5.50%), and weaker credit profile loans are pricing 5Y T+ 160s to 190s (~5.45-5.75%).
- Borrower demand is strongest for shorter duration debt with a spread add-on for more open period: +0-10 bps for last 12 months open, +20-25 bps for last 24 months open. To entice borrowers to consider longer duration, quoted spreads can be -20-25 bps tighter for 10Y loans.
- Floating rate for core profile, low leverage loans at SOFR+ high 100s to low-200s, 50 bps fee, 3+1+1.

INVESTMENT GRADE CORPORATE SPREADS

		Change			52 Week		
	10/10/2024	1 WK	1 MTH	YTD	Average	High	Low
IG Corp (bps to Treasuries)							
Cash Bond	96	-4 bps	-16 bps	-16 bps	110	142	96
7-10 Year Cash Bond	99	-5 bps	-18 bps	-23 bps	120	165	99

Source: J.P. Morgan

CMBS

- $77B YTD issuance is on pace to be one of the best years for CMBS volume post-GFC. Spreads have held steady at or near the tightest levels of the year across the curve, despite the deluge of bonds. CMBS bonds offer good relative value compared to corporates, which should help spreads tighten at the top of the stack. Lower rated tranches are also poised to tighten based on easing CRE credit concerns and a positive outlook for the economy.
- AAA conduit spreads are T+ 90-100, and AAA SASB spreads for the best profile deals are T+ 120s and SOFR+ 150s, but can range widely by asset class / profile into the high 100's.
- Lenders are quoting conduit coupons in the 6's% (5Y T+ 220-300 / 10Y T+ 180-250). Best full leverage fixed rate and floating rate SASB spreads are generally low to mid 200's over, depending on asset class and leverage, and deals perceived to be inferior price wider.
- Borrowers can "buy-down" the fixed 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		
	10/10/2024	1 WK	1 MTH	YTD	Average	High	Low
Conduit (bps to Treasuries)							
AAA 3 Year	80	-1 bps	-8 bps	-35 bps	99	137	80
AAA 5 Year	127	-1 bps	-11 bps	-48 bps	152	197	127
AAA 30% 10 Year	93	-2 bps	-1 bps	-32 bps	108	157	88
AAA 20% 10 Year	126	-3 bps	-20 bps	-69 bps	158	235	124
AA-	160	-6 bps	-14 bps	-73 bps	191	279	148
A-	185	-4 bps	-34 bps	-180 bps	279	456	185
BBB-	492	-6 bps	-72 bps	-386 bps	733	981	492

Source: J.P. Morgan

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CMBS NEW ISSUANCE							
Pricing Date	**Deal Name**	**Size ($MM)**	**Property**	**Term**	**Ext.**	**AAA**	**BBB-**
Conduit (bps to Treasuries) - Trailing 90 Days							
10/2/2024	BANK5 2024-5YR10	$837.8	NA	NA	NA	106*	550
9/27/2024	BANK 2024-BNK48	$1,090.8	NA	NA	NA	95	NAV
9/24/2024	MSC 2024-NSTB	$489.9	NA	NA	NA	165	NAV
9/19/2024	BMARK 2024-V10	$738.0	NA	NA	NA	110*	NAV
9/16/2024	BBCMS 2024-5C29	$1,065.4	NA	NA	NA	110*	495
9/10/2024	BMO 2024-5C6	$675.2	NA	NA	NA	117*	NAV
8/19/2024	BANK5 2024-5YR9	$910.2	NA	NA	NA	118*	560
8/16/2024	WFCM 2024-C63	$714.0	NA	NA	NA	104	510
8/14/2024	BMARK 2024-V9	$892.1	NA	NA	NA	123*	NAV
8/9/2024	BBCMS 2024-C28	$804.9	NA	NA	NA	106	NAV
7/31/2024	BMO 2024-5C5	$1,016.7	NA	NA	NA	115*	NAV
7/26/2024	BANK5 2024-5YR8	$690.5	NA	NA	NA	110*	NAV
7/16/2024	WFCM 2024-5C1	$731.9	NA	NA	NA	115*	570
SASB Floating (bps to SOFR) - Trailing 90 Days							
10/7/2024	WFCM 2024-GRP	$225.0	Retail	2	1,1,1	185	NA
10/1/2024	BX 2024-BRBK	$600.0	Office	2	1,1,1	300	610
9/30/2024	ARES 2024-IND2	$475.0	Industrial	2	1,1,1	150	275
9/27/2024	HIH 2024-61P	$423.6	Lodging	2	1,1,1	190	425
9/27/2024	SHR 2024-LXRY	$1,580.0	Lodging	2	1,1,1	195	445
9/20/2024	LBA 2024-7IND	$577.6	Industrial	2	1,1,1	150	270
9/12/2024	BX 2024-AIR2	$1,050.0	Multifamily	2	1,1,1	155	285
8/21/2024	ELMCL 2024-GTWY	$480.0	Industrial/Office	1	1,1,1	275	700
8/15/2024	HYT 2024-RGCY	$620.0	Lodging	2	1,1,1	190	350
8/8/2024	BAMLL 2024-BHP	$407.0	Lodging	2	1,1,1	235	450
8/7/2024	BOCA 2024-BOCA	$1,000.0	Lodging	2	1,1,1	198	370
8/6/2024	FS 2024-HULA	$400.0	Lodging	2	1,1,1	187	300
8/6/2024	AG 2024-NLP	$507.7	Industrial/Retail	2	1,1,1	227	NA
8/1/2024	WFCM 2024-MGP	$663.0	Retail	2	1,1,1	175/205	NA
7/25/2024	DBGS 2024-SBL	$344.5	Industrial	2	1,1,1	200	360
7/25/2024	NYC 2024-3ELV	$500.0	Multifamily/Retail	2	1,1,1	205	390
7/24/2024	KIND 2024-1	$517.0	Industrial/Office	2	1,1,1	195	350
7/23/2024	BX 2024-AIRC	$2,950.0	Multifamily	2	1,1,1	175	315
SASB Fixed (bps to Treasuries) - Trailing 90 Days							
10/9/2024	CSTL 2024-GATE	$463.0	Multifamily	5	NA	145	NA
10/7/2024	AHPT 2024-ATRM	$835.0	Lodging	5	NA	165	400
10/1/2024	NXPT 2024-STOR	$750.0	Self storage	5	NA	125	265
9/27/2024	LV 2024-SHOW	$850.0	Retail	5	NA	170	NA
9/17/2024	LEX 2024-BBG	$400.0	Office	4	NA	150	NA
9/16/2024	JPMCC 2024-OMNI	$307.0	Lodging	3	NA	150	NA
8/13/2024	LOEWS 2024-MIA	$305.0	Lodging	10	NA	150	NA
8/1/2024	GSMS 2024-RVR	$245.0	Multifamily	5	NA	145	NA
7/31/2024	BX 2024-BIO2	$516.7	Life Science	5	NA	150	400
7/25/2024	COMM 2024-277P	$650.0	Office	5	NA	200	NA
7/25/2024	EQT 2024-EXTR	$638.0	Industrial	5	NA	127	265

**5-Year AAA*

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Agency

- Agencies have been busy in September and October, fielding a record surge of deal flow from borrowers taking advantage of the September dip is Treasury yields. Since then, the Treasury rally faded sending yields to ~4% but agencies are still awash in deal flow, signing up deals at double the pace of 1H 2024. Higher Treasury yields will help spreads tighten. Agencies remain focused on mission-driven business but can still be competitive for best-in-class non-mission loans. Freddie is approaching its loan purchase cap ($70B), firm and funded $67B. Fannie is behind but has picked up the pace significantly and tracking to hit $45-50B by year-end.
- Fannie has been more aggressive for mission and underwriting parameters to boost inflows and catch-up, but Freddie is willing to push credit and pricing parameters to compete. Both are 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. Both are emphasizing property condition and sponsor diligence, digging into schedule of real estate owned to check portfolio performance and liquidity verification.
- Fixed rate spreads generally range from T+ 150-160s for mission and T+ 170-180s for non-mission (mid 5's% coupon), depending on sponsorship and deal profile. Longer duration 7-10Y spreads can be 5-10+ bps tighter.
- Borrowers prefer 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 very high 4's% to low-5's% interest rate.

AGENCY SPREAD SUMMARY

		Change			52 Week		
	10/10/2024	1 WK	1 MTH	YTD	Average	High	Low
Agency CMBS (bps to Treasuries)							
10/9.5 DUS TBA	57	-1 bps	2 bps	-8 bps	61	88	47
Freddie K A1	48	0 bps	-1 bps	-9 bps	55	81	45
Freddie K A2	49	1 bps	-2 bps	-9 bps	56	84	45
Freddie K B	120	-3 bps	-22 bps	-144 bps	209	303	120
Freddie K C	211	-4 bps	-28 bps	-153 bps	308	405	211

Source: J.P. Morgan

Bank

- Bank market share for new loan originations is at its lowest in 12 years but appears to have bottomed. Green shoots emerged earlier this year and bank appetite for CRE has continued to improve, especially from large domestic banks and foreign banks. Regional bank activity still seems to lag under balance sheet pressures except for scattershot outliers stepping up with aggressive quotes for strategic relationships. Recently there's been a notable shift in engagement from banks hungry for quality cash flowing term loans, but they face stiff competition from life cos and other non-bank lenders.
- Floating rate spreads for low leverage stabilized cash flowing deals are generally in the high 100s to low-200s over SOFR, translating to swapped interest rates in the mid 5's% range. More transitional profiles are mid-200s to 300 over SOFR.

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Debt Fund / Mortgage REIT

- Debt funds and other nonbank lenders remain active filling the gap left by the banks for bridge loans. Spreads have compressed YTD on improved availability and terms for back leverage.
- Banks have leaned-in to provide warehouse lines and note-on-note financing to debt funds at more favorable treatment than direct lending. The CLO market is still weak but there are signs market conditions are improving and new issuance is poised to rebound in 2025. Tighter CLO spreads and more issuance should pressure the banks to offer more competitive terms to debt funds resulting in tighter quoted spreads passed on to borrowers.
- Terms vary by profile, but the best pricing has tightened to SOFR+ mid 200s:
  - 60-70% LTC: mid 200s to low-300s spreads for preferred asset classes, in the lower half of the range with some in-place cash flow
  - 65-75%+ LTC: 300-400+ spreads for other asset classes / heavier lift business plan / riskier profile / weaker markets / small balance loans
  - Market SOFR floor is 3.00%
  - Notable change: some lenders have demonstrated a willingness to reduce call protection to 0-9 months

Construction

- The trajectory of lower interest rates and increased competition from lenders has led to improved leverage and pricing for quality construction loans. More banks are quoting spec non-recourse construction, along with select life companies and a deep field of debt funds. Leverage is up 5-10% from a year ago, spreads -25-50 bps tighter, and lenders are providing more flexibility around SOFR floors, and call protection.
- Construction loan transaction activity in 2024 has been light due to years of high borrowing costs, tighter credit availability and sidelined institutional equity, and softening fundamentals in certain markets. However, conditions are improving and declining interest rates and some relief in construction costs is helping fresh deals pencil. Developers are moving ahead on projects that make sense, hoping to deliver into an expansion cycle with more favorable fundamentals.
- Multifamily and spec industrial:
  - Non-recourse 50-55% LTC, SOFR+ 285-325, 55-60%+ SOFR+ 325-375
  - Partial recourse 60-65% LTC, SOFR+ 265-325
  - 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

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