Commercial Mortgage Alert A Green Street News Title

Banks Eye Transfer Deals To Lower CRE Risk

Many regional banks are exploring synthetic risk-transfer deals designed to reduce capital charges and to alleviate regulatory pressure tied to outsize commercial real estate portfolios.

Market players say the institutions have been making inquiries since last year as pressures started building, though talks would pause when conditions looked to be improving. Now, there is a growing belief that the deals finally will come.

"An increasing number of regional banks, particularly those with complex capital issues, are considering capital solutions," said **Stuart Goldstein,** co-head of **Cadwalader's** capital-markets practice.

Cadwalader partner **Jed Miller,** who has interacted with regulators on the transactions for years, noted that the level of interest is growing. "Our expectation is that we will see more banks executing this year and next," he said.

Stefanos Arethas, head of commercial real estate finance for **Atlas SP Partners,** said he has had talks with numerous banks looking to use credit-risk transfer to manage commercial real estate risk. But he downplayed the suggestion that there will be a vast transfer of exposure to weaker loans.

"The notion that there is all this stress out there and that issuers will use [credit-risk transfer deals] to transfer problem loans to the private market is a myth," he said. "CRT should be viewed as one tool in the toolbox that allows banks to retain assets on balance sheet and maintain client relationships and bring in new third-party capital. It's a slow, methodical repricing to the current interest-rate environment."

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THE GRAPEVINE

Kathleen Olin, a **CRE Finance Council** managing director who led several important industry initiatives, left her post in Washington earlier this month. Word on her next move could not be learned, but she's a market veteran who spent 13 years at **CWCapital** before joining CREFC in 2018. The industry group is interviewing potential replacements to work with its forums of servicers, investors, originators and other industry participants. In addition to interacting with such groups, Olin steered regular updates of the Investor Reporting Package.

Freddie Mac has tapped **Morningstar DBRS** veteran **Richard Carlson** to fill a role created as part of the agency's continued focus on property due diligence. He's

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Citi Tapped for Huge CMBS Refi of 53 Hotels

Citigroup is on track to originate a $631.5 million CMBS loan to refinance 53 hotels owned by a joint venture between **MCR** and **Building and Land Technology.**

The collateral for the three-year, fixed-rate mortgage, tentatively slated to be originated on April 11, would comprise 31 select-service hotels and 22 extended-stay properties in 14 states. The 5,958-room portfolio includes 33 hotels that operate under various Marriott flags, while the rest are affiliated with Hilton brands. **Eastdil Secured** arranged the financing.

Citi intends to securitize the interest-only mortgage via a single-borrower CMBS offering expected to price next week (HTL 2024-T53). The borrower will use $622.5 million of the proceeds to retire existing debt on the portfolio.

A Jan. 1 appraisal by **LW Hospitality Advisors** valued the collateral at $960 million, including a roughly 2.5% premium the properties would command if sold as

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Swanky NY Hotel Canvassing for Fresh Debt

The owner of a tony hotel on Manhattan's Upper East Side is looking for up to $350 million of debt to refinance a securitized loan it took out two years ago.

Alexico Group is talking to lenders about putting new debt on the 153-room Mark Hotel and the adjacent townhouse at 1000 Madison Avenue. The local shop, which owns several high-end hotels in the city, is considering loans at $325 million and $350 million of proceeds.

The request is for five years of term, and Alexico is open to either a fixed- or floating-rate coupon. **Newmark** is representing the owner, which controls the hotel and the townhouse building via a leasehold interest that runs until 2131.

The new debt would replace a $230 million floating-rate package originated in June 2022 that includes a $190 million senior mortgage securitized by **Credit Suisse** (CSMC 2022-MARK) and $120 million of mezzanine debt.

The 16-story hotel encompasses 106 rooms and 47 suites, including a penthouse suite dubbed the largest and most expensive in any North American hotel. Would-be

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The mechanics of such deals are relatively simple. An investor acting as a seller of insurance-like protection deposits cash in the amount of total potential losses with either the holder of the loans or a third party. The bank continues to service the loans and pays interest to the protection seller on that deposited money, akin to an insurance premium.

In the event of losses, however, the bank is made whole and stops paying interest on the amount of the deposit that is wiped out. If no losses occur by the end of the agreed-upon term, the

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full deposit is returned.

Market players involved in CRT discussions said that while many regional banks like the private nature of the transactions — allowing them to avoid dangerous headlines such as those that helped accelerate some bank failures last year — the loan portfolios they plan to reference are relatively pristine.

In fact, portfolios of loans backed by troubled office buildings or other distressed assets likely would be far too expensive to sell risk on, the sources said. One CMBS investor said he believes there is plenty of appetite for the deals and many good reasons for banks to do them other than to shed bad collateral.

"Even if you have to pay an investor 10% — and I'm just quoting a round number — that is a lot cheaper than raising equity or selling assets," he said. "But I would say there is not a great market for your distressed assets."

The only bank believed to have done a risk-transfer trade backed by private-label commercial real estate loans is **Merchants Bank of Indiana,** and it did so to free up capital to do more lending. The deal issued last year referenced a $1.2 billion portfolio of performing multifamily bridge loans destined for agency takeouts (MBHC 2023-CL1), with about 15% of first losses sold off.

New York Community Bank considered using the risk-transfer strategy when its shares tanked over a sagging real estate portfolio, but it instead found a deep-pocketed buyer in a group led by former Treasury Secretary **Steven Mnuchin.**

The Merchants Bank deal was structured as tradable notes issued via a special-purpose vehicle set up by the bank, but others are exploring even more hush-hush offerings that utilize credit-default swaps and are negotiated privately with one or several investors.

As in Europe, where such deals are more common, U.S. banks are looking for significant savings on capital charges applied by regulators without removing assets from their books. Transferring the bottom 12.5% of credit risk in a synthetic trade can lead to an 80% reduction, possibly slightly more, to the risk-based capital attributable to the synthetically securitized assets, Miller said.

And since regulators don't distinguish between stronger and weaker assets, there is little incentive to offload distressed risk. Market players believe any risk-transfer deals referencing commercial real estate portfolios will be picked over in much the same way B-piece buyers select assets in conduit deals.

Large banks such as **JPMorgan Chase** and **Citigroup** have used the strategy to offload billions of dollars of risk tied to auto loans and jumbo residential mortgages after U.S. regulators acquiesced to their use and issued Regulation Q in 2013 laying out some of the ground rules.

Interest broadened, however, after the **Federal Reserve Bank of New York** last September issued guidance that lawyers believe drew enough bright lines to get bank executives comfortable.

"As capital-management strategies, these trades have been endorsed by the regulators," Miller added, referencing the express mentions of "synthetic securitizations" in Regulation Q, the recent guidance and "reservation of authority" approvals the New York Fed started giving certain credit-linked note transactions last fall — none of which have been tied yet to commercial real estate.

Although regulators have been increasingly vocal about commercial real estate exposures, market players say they have been patient about applying pressure on banks to offload them. They believe that will start to change this year, however, hence predictions of an uptick in deal volume.

"Regulators are cracking down on the loan books of some of the smaller regional banks," said another CMBS investor who expects dealflow to pick up. "The solution they are being presented is CRT trades." ❖

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