

Customer Forward Thinking.[™]

Commercial Mortgage Commentary

CMLS Mortgage Analytics Group

Introduction

The Commercial Mortgage Commentary aims to inform the market on commercial real estate finance news. We focus on the following capital sources for commercial real estate: Conventional

Mortgages, CMHC-Insured Mortgages, Commercial Mortgage Backed Securities (CMBS), High Yield Mortgages, First Mortgage Bonds and Senior Unsecured debt for REITs and REOCs.

Making News

There were two headline transactions that occurred in Q1/2019:

Bentall Centre Sale

Blackstone Property Partners (BPP) and Hudson Pacific Properties purchased the four-tower Bentall Centre from China's Anbang Insurance Group. While the purchase price has yet to be disclosed, the deal is expected to be the most expensive real estate transaction in BC year to date. Anbang originally acquired the complex in 2016 for \$1.06 billion amidst allegations the deal circumvented Canadian laws around foreign ownership of key domestic assets. BPP will act

as managing partner with an 80% stake, while Hudson Pacific will oversee the daily operations as the operating partner with a 20% share in the property.

BCI/RBC Partnership

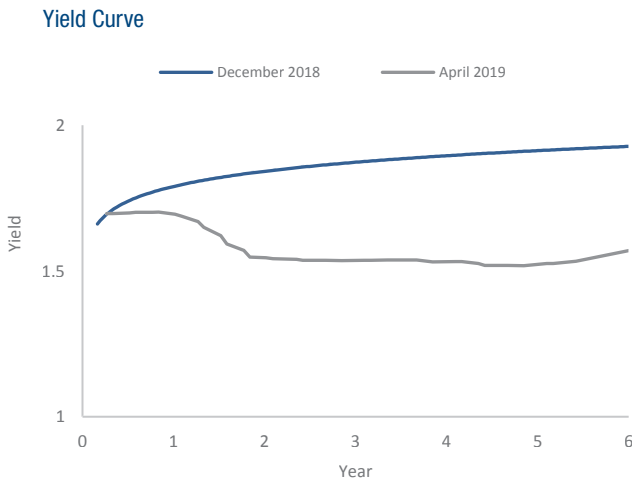
RBC Asset Management announced a \$7-billion agreement with BCI and QuadReal. This newly created fund will be one of Canada's most diversified commercial real estate portfolios and will include over 40 of BCI's current Canadian real estate assets. The fund is expected to open for investment in Q3/2019.

Economic Environment

The prevailing economic environment influences rates at which lenders are willing to provide capital. 2019 started off with a weaker economic outlook from the Bank of Canada (BOC), resulting mainly from the slowdown in the global economy and the fear of a recession.

The weaker prospects have resulted in a decrease in bond yields over the first quarter of 2019. Notably, the treasury yield curve inverted in late March for the first time since 2007, as the yield on a three-year bill traded higher than that of a 10-year bond.

An inverted yield curve is often associated with recessionary fears, as investors bid up the longer-term bond.



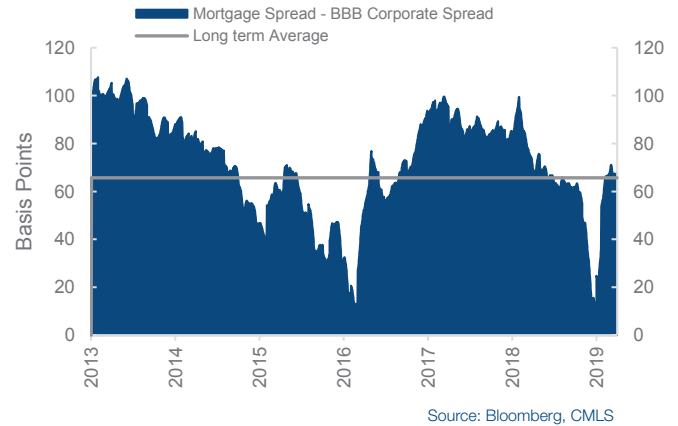
As expected, the Bank of Canada held its overnight target rate steady at 1.75% in its meeting in early March. However, there is growing sentiment that a rate cut is now on the table for 2019. The Bank of Canada raised its target rate three times in 2018.

Commercial Mortgages

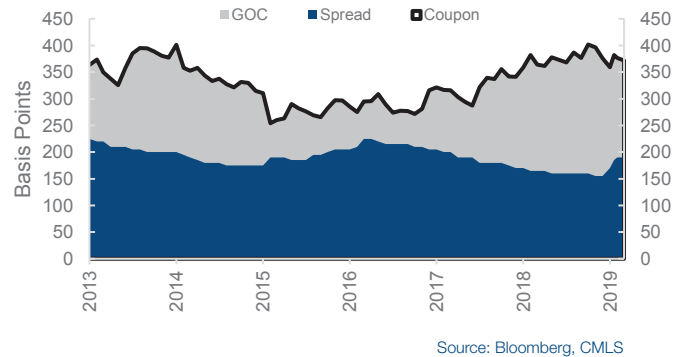
After a nearly 3-year period of declining commercial mortgage spreads, a significant shift took place as spreads rose sharply at the end of 2018 and beginning of 2019. In total, spread over GOC increased approximately 40 bps from Dec 2018 to Feb 2019. However, our Q1/2019 Canadian Commercial Mortgage Lenders Sentiment Survey indicates that most participants believe spreads will decline in the foreseeable future. Commercial spreads have started to ease at the end of Q1, with 5-year deals for top quality assets pricing at 170 to 190 bps above GOC.

The liquidity premium of commercial mortgage spreads over BBB-rated corporate spreads declined sharply in the latter part of 2018. This premium for 5-year loans started 2019 at 25 bps, but by the end of Q1, had risen back to 68 bps, slightly above the long-term average of 65 bps. The quick recovery of the commercial mortgage liquidity premium was a result of both a rise in commercial mortgage spreads and a drop in corporate spreads over GOC.

5-Year Commercial Mortgage Spread Premium Over BBB-Rated Corporate Bonds



5-Year Commercial Mortgage Spreads



CMHC

CMHC-insured mortgages are a popular financing option for apartment owners because of their low interest rates relative to non-government backed mortgages. The insured spreads have been relatively flat throughout Q1, with current spreads ranging from 85 bps to 95 bps for large, good quality assets.

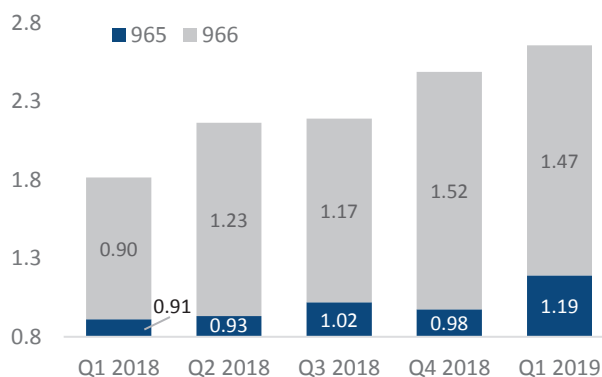
Most CMHC-insured lenders securitize loans using the NHA MBS and CMB programs. As a result, lenders quote spreads over the CMB rate, as opposed to the GOC yield. Through Q1/2019, the 5-year and 10-year CMB yield over GOC decreased from 42 bps to 40 bps and 55 bps to 46 bps, respectively. The lower CMB spread generally results in a lower overall credit spread over GOCs.

CMHC (continued)

CMHC-insured multi-family properties can be securitized in two NHA MBS pools: the 965 pool, which is comprised of fixed rate loans that allow prepayment with penalty; and the 966 pool, which does not allow prepayments.

The pools have increased significantly year-over-year, with the combined amount going from \$1.8 billion in Q1/2018 to \$2.7 billion in Q1/2019.

CMHC New Issuances (\$Billions)



Source: DBRS, Bloomberg

CMBS

In early April, we saw the first CMBS issuance of 2019. Real Estate Asset Liquidity Trust issued REAL-T 2019-HBC, a \$250-million CMBS comprised of 2 loans secured by Hudson’s Bay stand-alone

department stores located in Montreal and Ottawa. REAL 2019-HBC features a 4.229% weighted average interest rate, a 48-month weighted average term and AAA subordination of 16.875%. The LTC ratio is 46.7% due to the significant amount of cash equity (\$252 million) behind the subject loan.

Summary of recent CMBS deals

Year	Deal	Original Size (\$Millions, CAD)	# of Loans	# of Properties	Weighted Average DBRS Term DSCR
2019	REAL-T 2019-HBC	\$250	2	2	1.76x
2018	REAL-T 2018-1	\$352	63	72	1.40x
	CCMOT4 2018-4	\$550	53	53	1.33x
2017	REAL-T 2017	\$407	71	111	1.36x
2016	IMSCI 2016-7	\$352	38	60	1.47x
	REAL-T 2016-2	\$421	47	72	1.38x
	REAL-T 2016-1	\$401	55	91	1.30x
2015	CCMOT 2015-3	\$570	42	59	1.41x
	REAL-T 2015-1	\$335	46	46	1.50x
	IMSCI 2015-6	\$325	47	64	1.44x
2014	MCIC 2014-1	\$224	32	32	1.36x
	CMLSI 2014-1	\$284	37	37	1.47x
	REAL-T 2014-1	\$281	34	46	1.59x
	IMSCI 2014-5	\$312	41	55	1.44x

Source: DBRS, RBC

Senior Unsecured Debt

Senior Unsecured debt for REITs and REOCs is often an attractive substitute for conventional commercial mortgage financing. In Q1/2019, senior unsecured debt issuance reached \$1.175

billion, up from \$1 billion in Q4/18. Brookfield Property issued a \$350-million, 5-year debenture at a spread of 280.4 bps, which was 50 bps higher than their equal term issuance in Q3/2018.

Senior Unsecured Debt Issuances

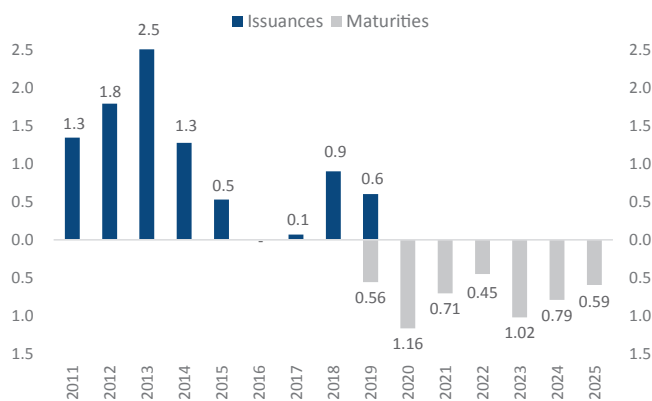
2019	Issuer Name	Issue Size (\$Millions)	Issuance Rating	Term (yrs)	Spread (bps)
Q1	SmartCentres REIT	350	BBB	2.25	111.9
	Artis REIT	250	BBBL	2	190
	Brookfield Property Finance ULC	350	BBB	5.05	247.7
	Morguard Corp	225	BBBL	5	280.4
Total/Average Q1		1,175		3.58	

First Mortgage Bonds

The First Mortgage bond market saw its first activity since Q1/2018 with an aggregate \$660-million bond on the Bay Wellington Tower in Toronto. The tower features 47-storays and 1.4 million square feet, with a LEED Gold certification.

Issued by Brookfield Office Properties, the bond is comprised of \$270 million Series A: 7-year, 3.299% coupon and \$390 million Series B: 10-year, 3.464% coupon. Both series feature a 5-year interest only period and a 30-year amortization.

First Mortgage Bond Issuances and Maturities



Source: Bloomberg, CMLS

ABOUT CMLS MORTGAGE ANALYTICS GROUP

The CMLS Mortgage Analytics Group is a division of CMLS Financial Ltd., and is one of the only independent, dedicated providers of mortgage valuation services and software for the commercial real estate finance industry in Canada. The CMLS Mortgage Analytics Group provides solutions to some of Canada's most prominent financial institutions, investment managers, pension funds and consultants. With investors, regulatory bodies and governing committees requiring increased reporting, independence and third-party advice, the CMLS Mortgage Analytics Group offers a host of risk rating, valuation, and portfolio analysis tools to better manage risk/reward profiles in commercial mortgage portfolios. Clients engage our services to provide independent support for mortgage purchases, fair value accounting, ongoing fund valuation, interest rate appraisals and more.

ERIC CLARK, CFA
 Managing Director
 604.488.3897
 eric.clark@cmls.ca

SUKHMAN GREWAL, CFA
 Associate Director
 604.235.5110
 sukhman.grewal@cmls.ca

COLIN LEE, CFA
 Senior Market Analyst
 604.637.0166
 colin.lee@cmls.ca

RESEARCH TEAM:
 Meeran Amir
 Joanne Zhao
 Max Schriber



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