

# Customer Forward Thinking.™

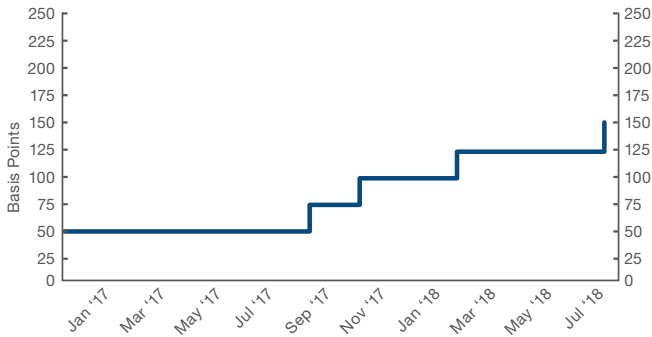
# Commercial Mortgage Commentary

## Making News

### Overnight Rate

After holding steady in April, the Bank of Canada (“BOC”) elected in the July meeting to increase the overnight target rate by 25 bps to 1.50%. Prime lending rates across the major Canadian banks followed suit with a 25 bps increase to 3.70%. After the news broke, swap markets were pricing a 66% probability of a third hike before the new year.

BOC Overnight Target Rate

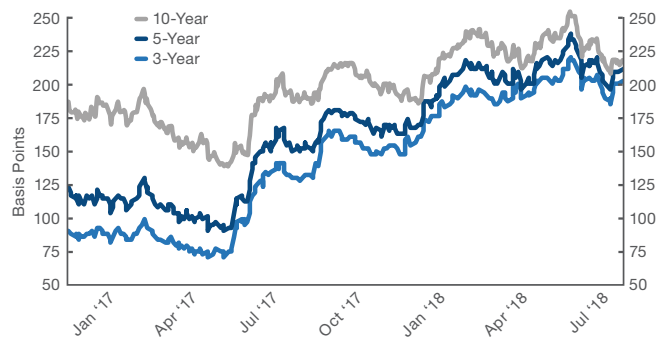


Source: Bloomberg, CMLS

### GOC Yields

Government of Canada (“GOC”) bond yields continued to flatten through Q2/18 as shorter-term spreads climbed relative to longer-term. The premium between the 3-year and 10-year tightened by 4 bps and the premium between the 5-year and 10-year tightened by 5 bps.

Historical GOC Yields



Source: Bloomberg, CMLS

### Investments

Three REIT equity offerings occurred in Q2/2018 totaling \$700 million. In June, Dream Global REIT (TSX: DRG.UN) and Allied Properties REIT (TSX:AP.UN) raised \$201 million and \$299 million, respectively. In July,

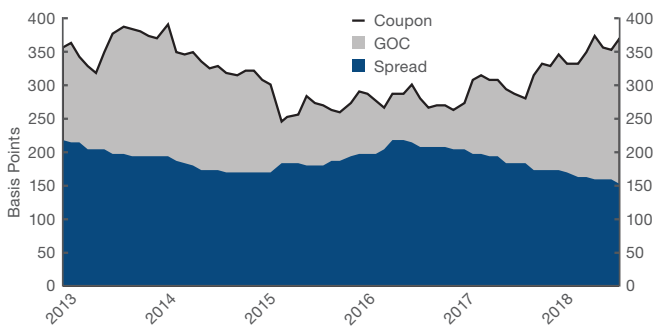
Minto Apartment REIT (TSX: MI.UN) completed a CAD\$ 200 million IPO. The IPO funded the indirect acquisition of 22 multi-unit residential properties from a related Minto group company, which was comprised of 4,279 suites located in Toronto, Ottawa, Calgary, and Edmonton.

# Commercial Mortgages

Since our May Commentary, lender appetite for high quality commercial mortgages remained balanced with borrower demand, causing spreads to remain flat. 5-year deals are pricing at 145 bps to 160 bps for top quality assets, while 10-year spreads maintain a 10 bps premium for similar risk. With stagnant commercial mortgage spreads, the upward trend on

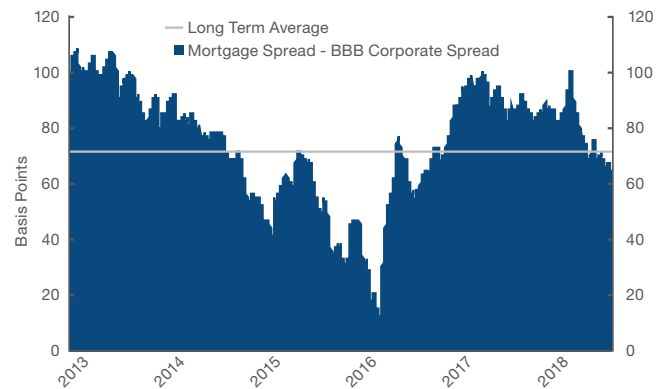
BBB-rated corporate bonds reduced the commercial mortgages liquidity premium by 21 bps since the beginning of 2018. With the spread premium now below the long-term average, commercial mortgage spreads would need to climb, or BBB-rated corporate spreads would need to fall to move the premium in-line with the long-term average.

5-year commercial mortgage spreads



Source: Bloomberg, CMLS

5-year commercial mortgage spread premium over BBB-rated corporate bonds



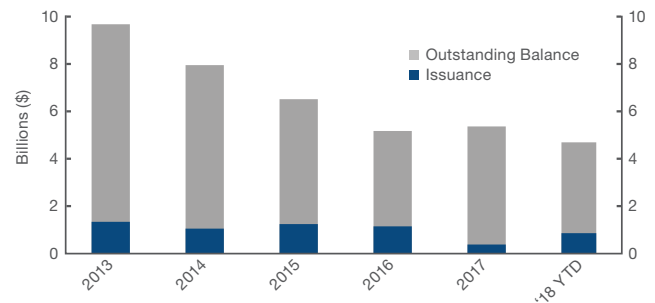
Source: Bloomberg, CMLS

## CMBS

The second CMBS issuance of 2018 occurred early in Q3/18. RBC marketed REAL-T 2018-1, a \$352 million CMBS comprised of 63 loans, secured by 72 properties. Most of the properties in the latest REAL-T are in Quebec followed by Ontario. The geographical concentration is similar to that of the March 2018 CMBS issuance of CCMOT 2018-4.

REAL-T 2018-1 features a 4.28% weighted average interest rate, an 88-month weighted average remaining term, and AAA subordination of 13.125%. The issuance brings the total outstanding balance of CMBS loans to \$5.62 billion with \$493 million scheduled to mature in 2018.

CMBS balance outstanding and issuance



Source: DBRS, Bloomberg

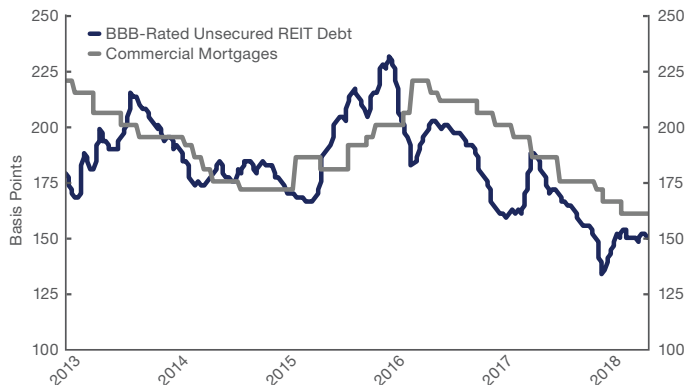
# Senior Unsecured Debt

Senior unsecured debt issued in Q2/18 slowed to \$1.65 billion, down from \$2.9 billion in Q1/18. However, cumulative 2018 issuance is up 32% on a YTD basis over 2017 and makes up 80% of the total issuance in 2017.

Two of the five issuances in Q2, totaling \$800 million, were from OMERS Realty Corporation. This included a \$550 million 12-year and a \$250 million 7-year note with spreads of 116 bps and 94 bps, respectively. Early in Q3/18, a single \$300 million 5-year note was issued by Brookfield Property Finance ULC. Spreads on BBB-rated unsecured REIT debt remained stable through Q2/18 at 150 bps.

Spreads on unsecured REIT debt remain cheaper than those on conventional commercial mortgages. As investor demand for senior unsecured debt remains available to the market, REITs continue to enjoy cheaper unsecured financing.

Spreads on BBB-rated unsecured REIT debt vs. commercial mortgages



Source: Bloomberg, CMLS

## Senior unsecured debt issuances

2018	Issuer Name	Issue Size (\$Millions)	Issuance Rating	Term (yrs)	Spread (bps)
Q1	Choice Properties	350	BBB	7	143.4
	Choice Properties	300	BBB	4	103.5
	Riocan	250	BBBH	5	139.2
	H&R REIT	300	BBBH	5.5	106.9
	CT REIT	200	BBBH	10	159.1
	Artis REIT	200	BBBL	2	CDOR+107
	Choice Properties	750	BBB	10	196.8
	Choice Properties	550	BBB	6.5	146.5
Total/Average Q1		2,900		6.25	
Q2	Ivanhoe Cambridge II Inc.	500	AAL	5	89.4
	OMERS Realty Group	550	AAL	12	115.9
	OMERS Realty Group	250	AAL	7	93.6
	Morguard Corp	200	BBBL	3	202
	Chartwell Retirement Residences	150	BBBL	7	189.5
Total/Average Q2		1,650		6.69	
Q3	Brookfield Property Finance ULC	300	BBB	5	230.5
Total/Average Q3		300		5.00	
<b>Total/Average YTD 2018</b>		<b>4,850</b>		<b>6.32</b>	

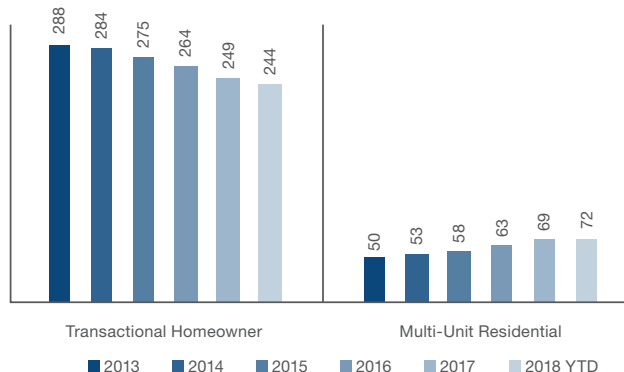
Source: Bloomberg

# CMHC

The Canada Mortgage and Housing Corporation (“CMHC”) continues to reduce its exposure to homeowner insurance as a result of the tighter federal mortgage rules, which was partially offset by an increase in multi-unit apartment building insurance. The Insurance-in-Force (“IIF”) for homeowner insurance has decreased \$44 billion to \$244 billion from 2013 to Q2/18, while the multi-unit IIF increased \$22 billion to \$72 billion for the same period. Amidst higher real estate and rental prices across the country, CMHC will continue to place a focus on rental housing programs.

CMHC-insured spreads remained flat between 80 bps and 105 bps over GOC on 5-year terms and between 85 bps and 110 bps over GOC on 10-year terms. All-in coupons increased roughly 10 bps from increases in the GOC.

Insurance-in-Force size



Source: CMHC

## ABOUT CMLS FINANCIAL LTD.

CMLS Financial Ltd. is a diversified provider of lending products and services to the commercial and residential real estate finance industry. We take great pride in continuing our over forty year tradition of exceptional service to borrowers, lenders, mortgage bankers and brokers. CMLS Financial is one of the only independent, dedicated providers of mortgage services for the commercial real estate finance industry in Canada.

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