Commercial Mortgage-Backed Securities

Opportunities in Senior Securities with Enhanced Credit Features

This report is excerpted from the Third Quarter 2025 Fixed-Income Sector Views.

Navigating CMBS market complexities amid volatility and legacy issues.

Commercial real estate remains an extremely bifurcated market. However, as in other IG credit sectors, April's volatility did little to slow the CMBS market's momentum, with spreads tightening quarter over quarter and new issuance volumes reaching a post-Global Financial Crisis high. This trend seems technically driven rather than fundamentally justified, given cap rates generally are less than 0.5 percent above mortgage rates. Legacy issues persist, with less than half of office loans in conduit CMBS refinancing on schedule. Therefore, subsector allocation and security selection are crucial to navigating CMBS market complexities and risks.

Sector Commentary

- Non-Agency CMBS issuance reached $75 billion through the second quarter of 2024, marking a 68 percent increase compared to the same period last year.
- Issuance trends from the previous quarter persisted, with a focus on single asset/single borrower (SASB) transactions, as investors prefer large loan deals for concentrated positioning.
- Office-backed deals accounted for 28 percent of total SASB issuance, driven by investor interest in financing offices in Tier 1 sub-markets, notably New York City.
- Despite healthy new issuance, the seasoned CMBS universe faces challenges. The serious delinquency rate for conduit CMBS loans rose by 0.9 percentage points year to date, reaching 7.3 percent, with office loans hitting 12.4 percent.

Investment Themes

- We maintain our preference for senior securities with higher credit enhancement, capable sponsorship, and limited exposure to legacy real estate issues, such as most offices, and to market cyclicality, including certain hotels.
- Most mezzanine and junior bonds across commercial CMBS subsectors do not adequately compensate investors at current levels.
- Select commercial real estate collateralized loan obligation (CRE CLO) transactions, particularly those backed by top-tier real estate investment trusts (REITs) and debt funds, and SASB deals, especially those backed by well-located apartments or well-tenanted data centers, continue to offer attractive risk-adjusted returns compared to other fixed-income sectors in our view.

By Tom Nash and Hongli Yang

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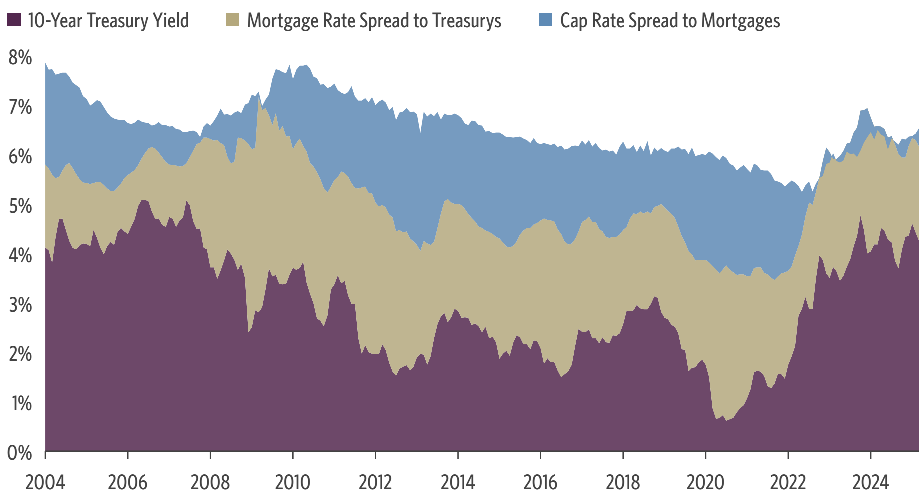
Cap Rate Spreads Over Mortgage Rates Remain at 20-Year Lows

Blended Core CRE and Multifamily Cap Rate Spreads to Mortgages, Treasurys



Source: Guggenheim Investments, MSCI Real Assets, JP Morgan. Data as of 6.30.2025.

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Investing involves risk, including the possible loss of principal. In general, the value of a fixed-income security falls when interest rates rise and rises when interest rates fall. Longer term bonds are more sensitive to interest rate changes and subject to greater volatility than those with shorter maturities. During periods of declining rates, the interest rates on floating rate securities generally reset downward and their value is unlikely to rise to the same extent as comparable fixed rate securities. High yield and unrated debt securities are at a greater risk of default than investment grade bonds and may be less liquid, which may increase volatility. Investors in asset-backed securities, including mortgage-backed securities and collateralized loan obligations ("CLOs"), generally receive payments that are part interest and part return of principal. These payments may vary based on the rate loans are repaid. Some asset-backed securities may have structures that make their reaction to interest rates and other factors difficult to predict, making their prices volatile and they are subject to liquidity and valuation risk. CLOs bear similar risks to investing in loans directly, such as credit, interest rate, counterparty, prepayment, liquidity, and valuation risks. Loans are often below investment grade, may be unrated, and typically offer a fixed or floating interest rate.

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