

Commercial Mortgage-Backed Securities Strong Demand, But Not for WeWork



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Liquidity remains strong after the largest post-crisis SASB and CRE-CLO deals.

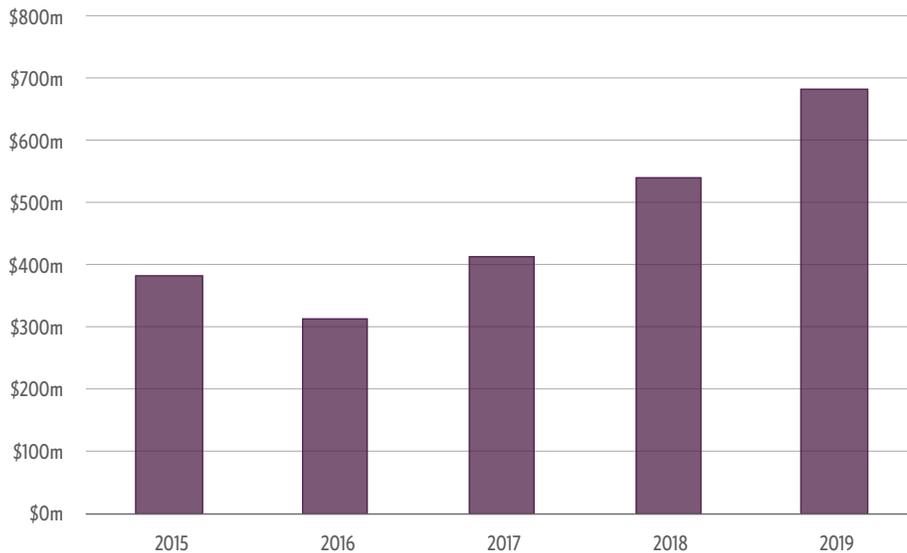
The CMBS sector continued to enjoy healthy liquidity despite new issue deal sizes growing larger in the third quarter. The largest post-crisis single-asset/single borrower (SASB) deal was issued at a staggering \$5.6 billion. The deal was announced and closed in less than one week, showing the strength in demand. The deal creates a new benchmark for the SASB world as there were six co-managers on the deal and each of these dealers is making daily markets on the entire capital stack. Usually, the SASB market is more bespoke, with only a few dealers specializing in certain deals. In CRE-CLO, two transactions priced at over \$1 billion, including the largest CRE-CLO issued to date at \$1.2 billion. The market received both deals well, with spreads remaining relatively unchanged from previous issuances. As a result of the success of these larger transactions, we expect the average CRE-CLO pool size to continue to grow in 2020 (see chart, top right). Lastly, conduit liquidity remains strong, with as many as 10-15 dealers actively bidding on investment-grade bid lists.

The CMBS world was focused on WeWork's IPO withdrawal, its halting growth, and its cost cutting efforts, leading to speculation of potential defaults on their debt obligations and lease payments. A large portion of WeWork's portfolio is in New York, specifically midtown Manhattan (see chart, bottom right). If WeWork needed to reduce its occupied space, Midtown office rents could decline, and cap rates could rise. We have consistently maintained a bearish view on WeWork due to its business model of mismatching short-term assets with long-term liabilities. Additionally, the diversification in conduit bonds means that no one obligor can have a large impact to the overall transaction. The credit enhancement of investment-grade bonds provides additional protection from losses on any one loan.

While secondary liquidity is stable and credit metrics have remained relatively unchanged in new issue deals, we continue to be cautious about investing in conduit transactions as spreads are close to post crisis tights.

Average CRE-CLO Pool Size Should Continue to Grow in 2020

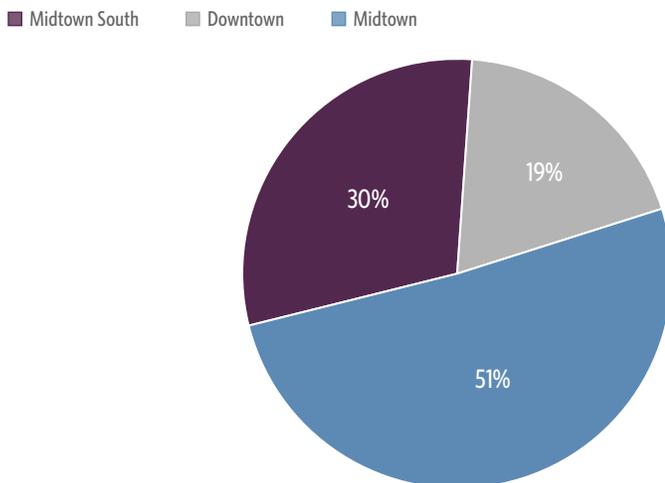
CRE-CLO Average Pool Size by Year



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A Contraction in WeWork's Manhattan Portfolio Could Trigger Higher Cap Rates

WeWork's Manhattan Portfolio



A large portion of WeWork's portfolio is in New York, specifically midtown Manhattan. If WeWork needed to reduce its occupied space, Midtown office rents could decline, and cap rates could rise.

Source: Guggenheim Investments, Morgan Stanley. Data as of 9.30.2019.

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