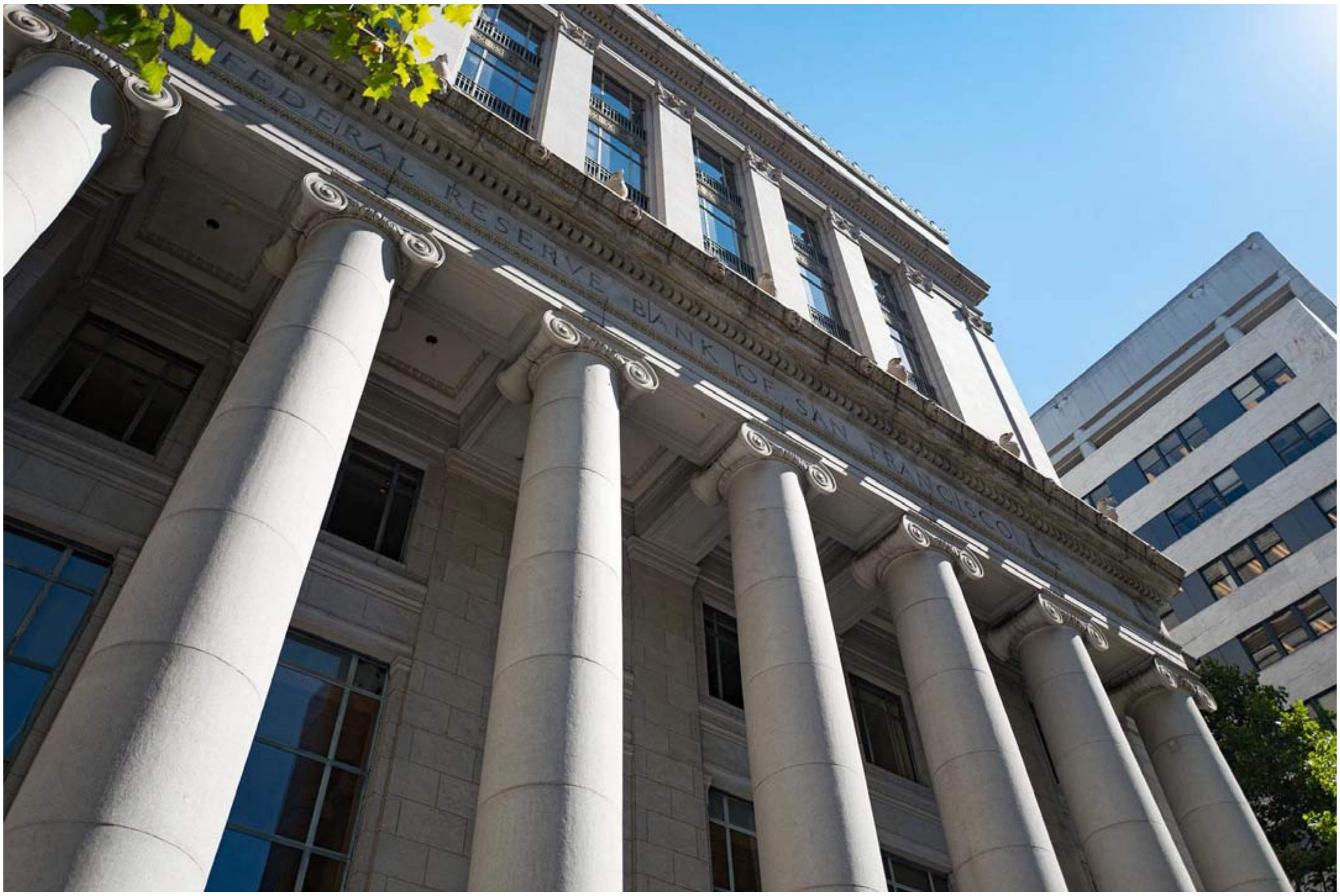
Outlook Worsens for Commercial Real Estate Finance Industry

CREFC Survey Shows Fifth Consecutive Quarterly Decline in Sentiment



In a new survey, the commercial real estate finance industry voiced concerns about high interest rates set by the Federal Reserve. (Getty Images)

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CoStar News

November 9, 2022 | 4:34 P.M.

The downbeat attitude on the outlook for commercial real estate finance worsened in the third quarter, professionals said in a new survey.

Concerns are coming from several now-familiar fronts, according to the CRE Finance Council, the association that represents the $5.4 trillion industry. There's uncertainty about financing when it comes to inflation, rising interest rates and the looming potential for a global recession, CREFC reported in its third-quarter Board of Governors Sentiment Index.

The index captures the pulse of various industry constituents, including balance sheet and mortgage bond lenders, loan and bond investors, private equity firms, debt funds, servicers and rating agencies.

Overall sentiment dropped from 70.7 in the second quarter to 61.4 in the third, a decline of 13%. This is the fifth consecutive quarterly drop and follows a 12% drop in overall sentiment from the first quarter to the second.

“This most recent survey accurately captures the concerns of the industry at large at this time,” CREFC Executive Director Lisa Pendergast said in a statement. “The shape of the commercial real estate debt market changed very quickly in the third quarter, and the surveyed responses reflect that swift shift.”

The questions posed to the survey participants that saw the most significant movements were around expectations for commercial real estate fundamentals, and the impact of trends in commercial mortgage-backed securities and commercial real estate collateralized loan obligations on demand and pricing.

Real estate fundamentals are expected to worsen, according to the survey. Sentiment shifted from 34% of respondents calling fundamentals negative in the second quarter to 83% in the third — a 49-point jump.

For the second quarter, 49% of respondents said demand and pricing for bonds would be negative. That result increased to 75% in the third quarter.

The latest survey included two open-ended questions. The first asked respondents’ opinion on future distress in commercial real estate loans. Most responses indicated that upcoming loan maturities would drive special servicing rates and losses higher.

However, some respondents said that losses would be muted, given the amount of cash waiting to be invested, disciplined underwriting and value creation over the past 10 years.

In addition, participants were asked about the potential for the United States to experience a recession in late 2022 to 2023. About 92% answered in the affirmative.

“We remain optimistic, however, that despite the increased likelihood of a recession, we are in a much better position and stronger place than we were as an industry in 2008,” Pendergast said.