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**Contacts****Jeff Adler**

*Vice President & General  
Manager of Yardi Matrix*  
Jeff.Adler@Yardi.com  
(303) 615-3676

**Jack Kern**

*Director of Research and  
Publications*  
Jack.Kern@Yardi.com  
(800) 866-1124 x2444

**Paul Fiorilla**

*Director of Research*  
Paul.Fiorilla@Yardi.com  
(800) 866-1124 x5764

**Chris Nebenzahl**

*Editorial Director*  
Chris.Nebenzahl@Yardi.com  
(800) 866-1124 x2200

# CMBS Takes a Punch, Hits Back at Critics

A decade into a cycle with outstanding CMBS performance, a group of critics has emerged to allege widespread impropriety in the loan origination process. The critics—amplified by major media—say that CMBS issuers routinely embellish loan documents to exaggerate the performance of underlying properties.

CMBS insiders strongly deny the charges and note that transparency has been a top theme of the industry post-financial crisis. Indeed, CMBS collateral is subject to more rigorous disclosure of information than virtually any other securitized product.

Industry players say the evidence that lessons were taken to heart is in loan performance. Since the chastened market reformed a decade ago, post-financial crisis issuance—dubbed CMBS 2.0—was nothing short of stellar until the pandemic. As of the first quarter of 2020, only 1.8% of CMBS loans were 30 days or more delinquent, the lowest level since the fourth quarter of 2008, per Wells Fargo and Intex.

Whether through luck or design, the reports alleging malfeasance came just as the impact of COVID-19 hit and loan defaults suddenly shot up. The CMBS delinquency rate spiked to 9.6% as of July, according to Trepp, almost entirely because of sharp increases in hotel and retail loans. Depending on one's vantage point, that either supports the claims or gives credence to questions about whether they are being promoted to help industry litigation consultants gin up business as loan defaults increase.

To date the allegations have had little impact, as the market is preoccupied dealing with the growing number of delinquencies, trying to drum up loans while transaction activity is down and lobbying for COVID-19 relief. But if loan delinquencies continue to rise—whether caused by sloppy underwriting or not—the drumbeat of criticism is likely to grow.

## Studies Allege Improprieties in Underwriting

The first shot came in May from an article in ProPublica that outlined allegations made in a whistleblower complaint filed with the Securities and Exchange Commission by John Flynn, the chief executive of CRE Loan Advisors, a consulting firm for distressed commercial borrowers. In the article,