



Federal Reserve Bank of Dallas (the
“Bank”) and The Robert and
Margaret Folsom Institute for Real
Estate at SMU

**Financing: Challenges &
Opportunities –
May 8, 2024**

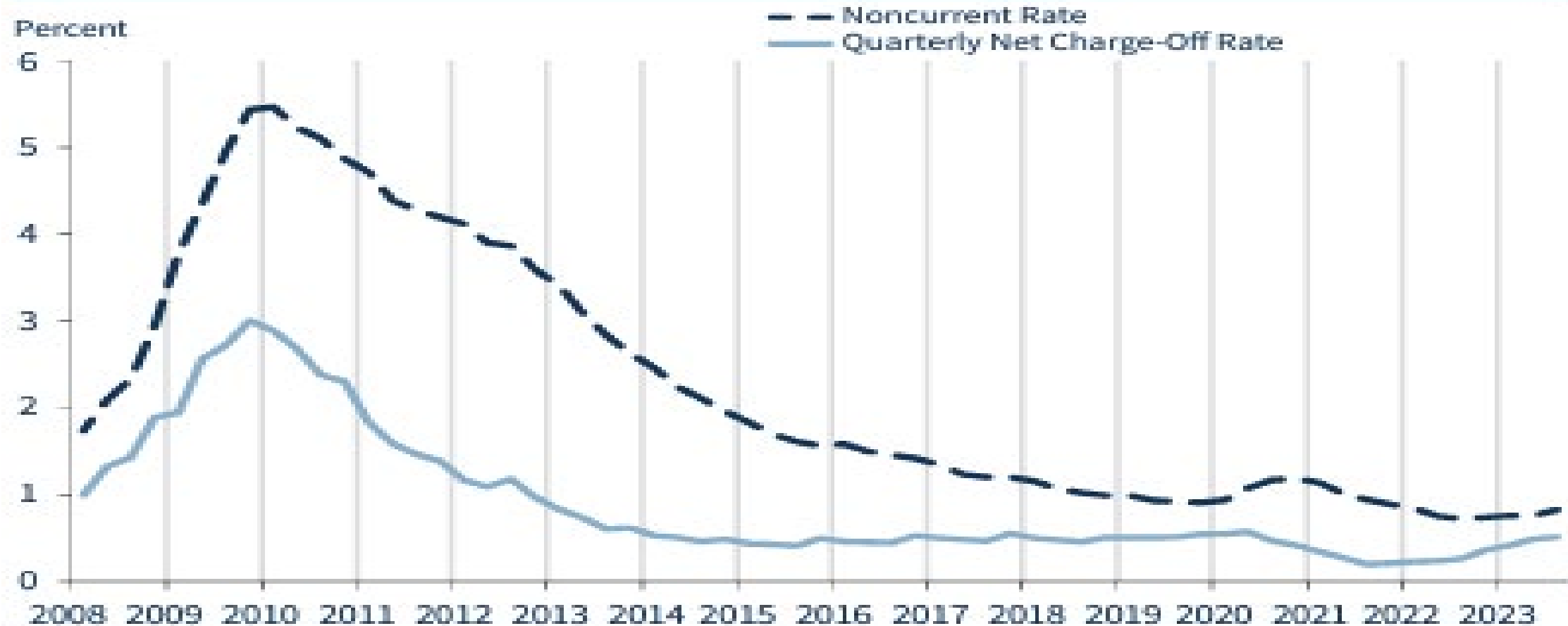




- **Merrill J. Reynolds- Managing Director Certified Community Bank Directors Program – Southwestern Graduate School of Banking**

Noncurrent Loan Rate and Quarterly Net Charge-Off Rate

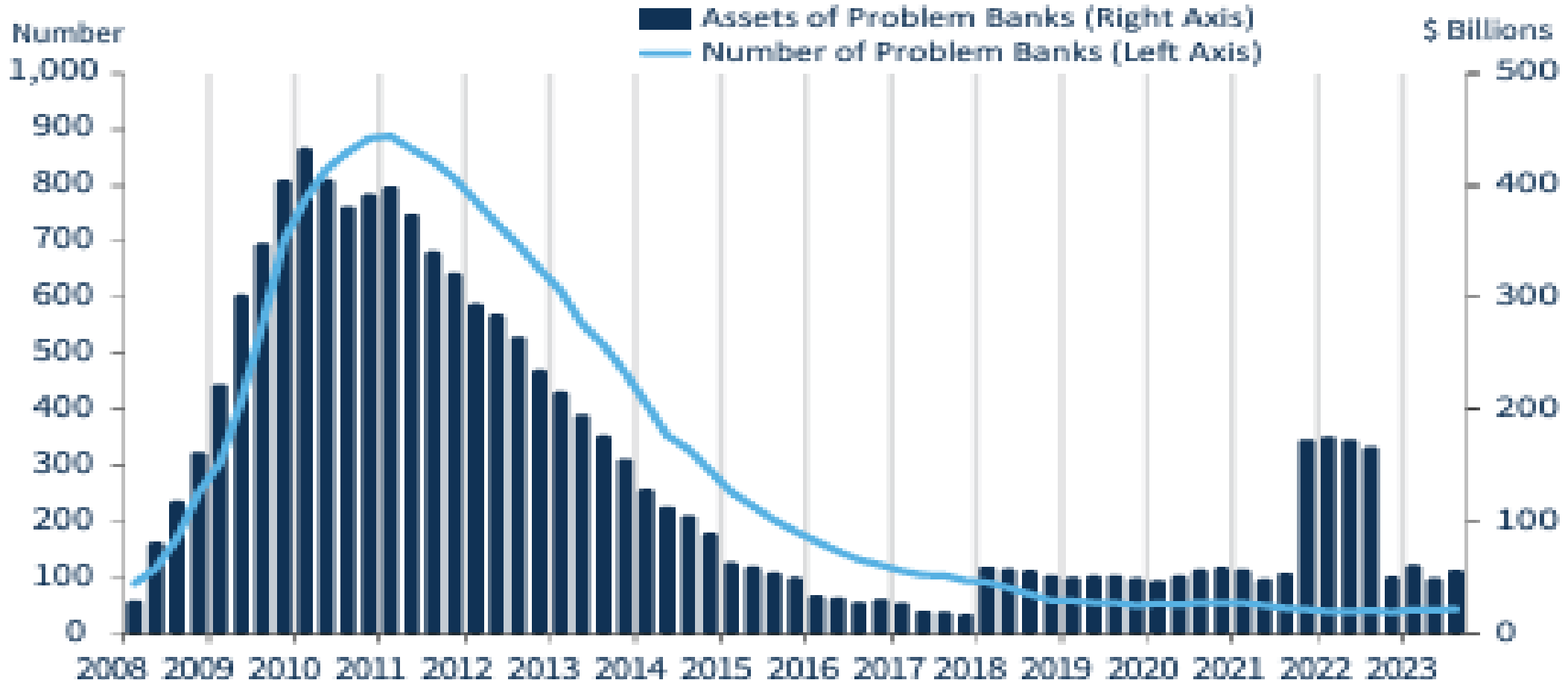
All FDIC-Insured Institutions



Source: FDIC.

Number and Assets of Banks on the “Problem Bank List”

All FDIC-Insured Institutions



Source: FDIC.

Note: The asset values of insured financial institutions on the problem bank list are what were on record as of the last day of the quarter.

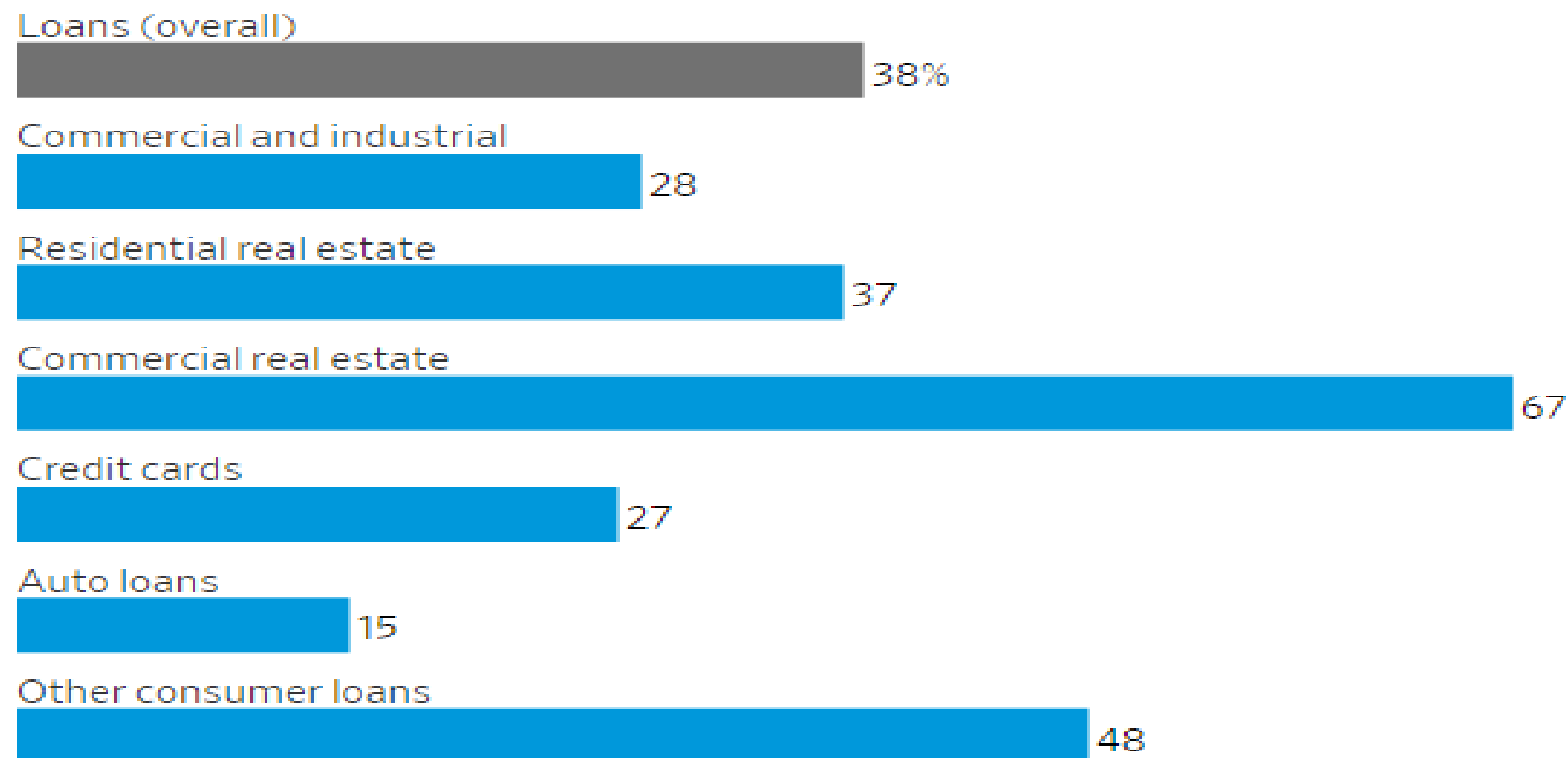
\$929 billion

- That's the estimated value of the outstanding U.S. commercial and multifamily debt set to mature this year, nearly 20% of all outstanding debt of its kind. The figure is 40% higher than the Mortgage Bankers Association's original estimate of \$659 billion. Fueling the surge have been loan extensions—many loans with 2023 maturity dates were not paid off—and other delays that are now coming to an end, not new transactions. Banks own \$441 billion of commercial-property debt coming due this year.

Source: The Real Deal Real Estate News.

Smaller Lenders

Small and medium-size banks' share of all outstanding loans, by type



Note: Small and medium-size banks are domestically chartered banks that are smaller than the top 25 lenders

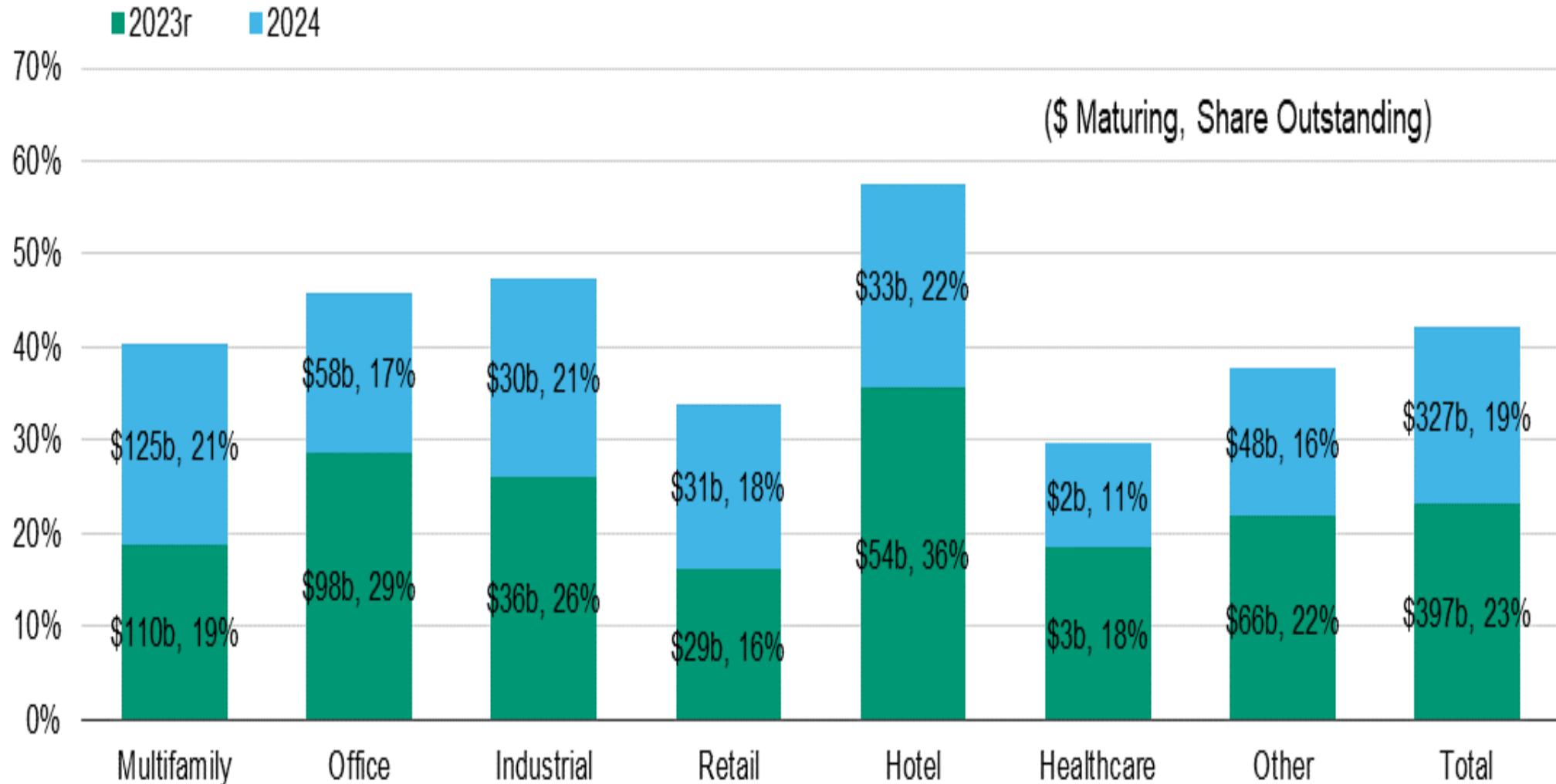
Source: Federal Reserve

Overall Share of Banks' Assets Exposed to CRE Loans

Bank Category	Multifamily CRE Loans	Commercial CRE Loans	Funded CRE Construction Loans	Total Direct CRE Exposure	Indirect CRE Exposure*	Total CRE Exposure
Fed "Large" Banks (25 banks, >\$160B total assets)	1.4%	2.2%	0.8%	4.3%	2.5%	6.8%
Regional Banks (135 banks, \$10-160B total assets)	4.7%	8.3%	3.5%	16.5%	9.8%	26.3%
Community Banks (829 banks, \$1-10B total assets)	5.5%	13.3%	5.4%	24.3%	13.5%	37.7%
Small Banks (2,965 banks, \$100mm-1B total assets)	2.9%	10.1%	5.2%	18.3%	12.5%	30.7%
Small Banks (761 banks, <\$100mm total assets)	0.9%	3.9%	2.5%	7.2%	5.4%	12.6%
Total (4,715 banks)	2.5%	4.9%	2.0%	9.4%	5.5%	14.9%

Source: Moody's.

Bank Loan Maturities, by Property Type, through 2024



Source: Moody's.

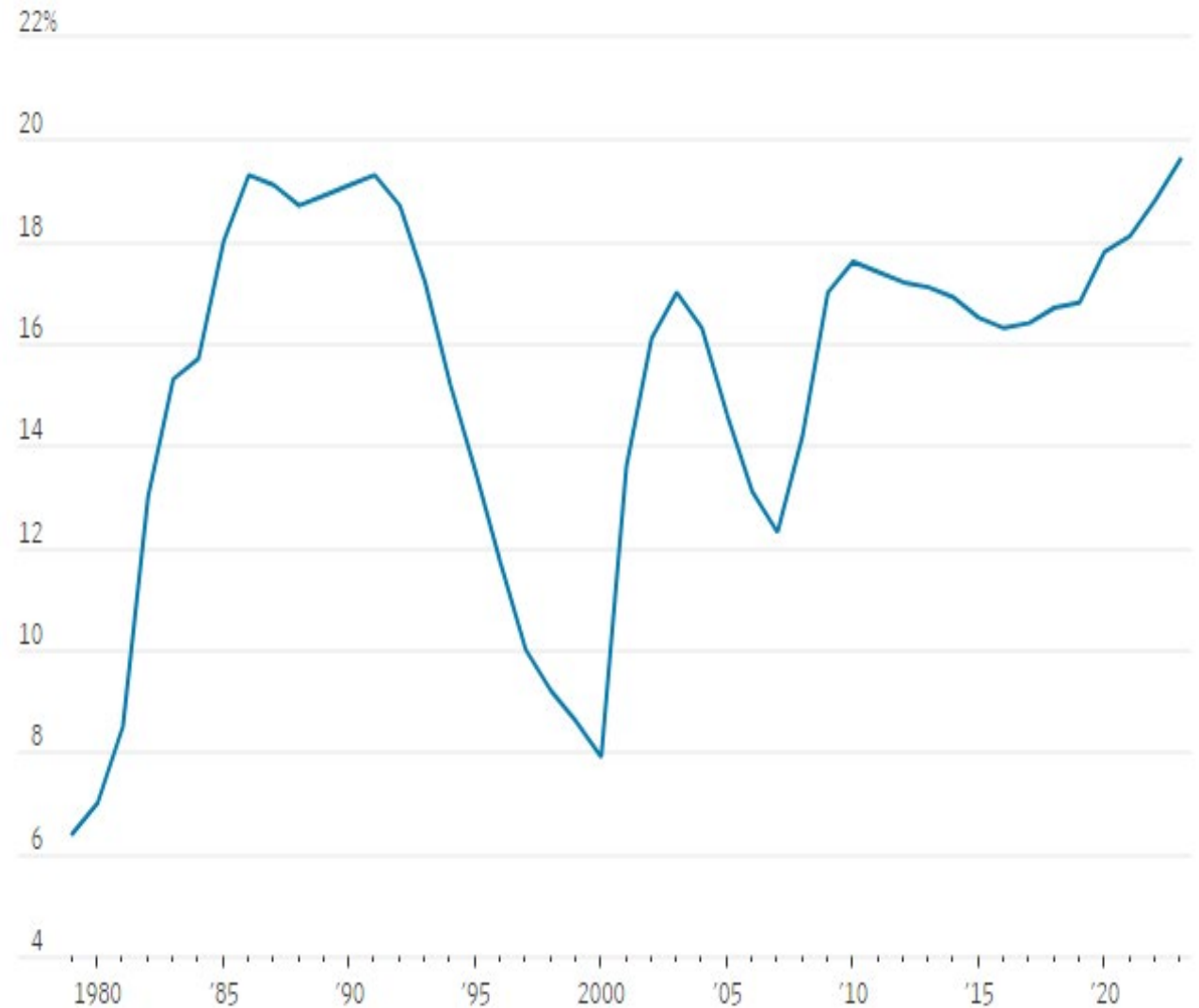
WSJ – 10/9/23

- America's highest office vacancies aren't in the East and West Coast cities that have been shedding population and workers. They are in Texas, a thriving Sunbelt state that has been luring companies away from the big coastal cities.
- Houston, Dallas and Austin top the list of major U.S. cities with the highest office-vacancy rates, according to Moody's Analytics. About 25% of their office space wasn't leased as of the third quarter. That was more than double New York's vacancy rate of 12% and well above San Francisco's vacancy rate of 17%.

- Real estate values for most property types are unlikely to stabilize until mid-2024. Cap rates, excluding those for office assets, increased by roughly 150 basis points between early 2022 and late 2023 depending on market and asset type. This would imply a 20% decrease in values for most property types. Cap rates could expand by an additional 25-50 basis points in 2024, with a corresponding 5% to 15% decrease in property values.
- Appraisals and Evaluations are critical on renewals, extensions and criticized loans.
- Stress Testing continues is critical and expected.

- A staggering 19.6% of office space in major U.S. cities wasn't leased as of the fourth quarter, according to Moody's Analytics, up from 18.8% a year earlier. That is slightly above the previous records of 19.3% set in 1986 and 1991 and the highest number since at least 1979, which is as far back as Moody's data go.

U.S. office-vacancy rate



Source: Moody's Analytics

Proactive Management

- Understand your maturing loan portfolio and what increased rate scenarios are going to impact DSC of your customer.
- Understand on commercial real estate what the current occupancy and usage of the building is prior to renewal of the loan.
- Understand what rent concessions are doing to the value of a property. Note the dramatic increase in operating costs (Taxes and Insurance) that are heavily weighing on the NOI. There are projects where the EGI is higher than underwriting but the increases in operating costs outpaced the rent increases resulting in a lower NOI. Couple that with rate increases and we are seeing inadequate or marginal DSC. This is mostly hitting the deals underwritten in 2020 and 2021.

- How the Bank identifies and tracks projects that are not yet stabilized. What dollars the Bank has exposed to projects that are not yet stabilized? Identifying these and monitoring lease-up compared to underwriting and appraisal is key. It would also be good to understand the valuation of non-stabilized projects.
- A strong economy is helping to delay the day of reckoning, as most tenants are still paying the rent. Pressure is building slowly as leases expire. Many companies are reducing their space by 30% to 40% when their contracts end.
- Loan Extensions are acceptable provided the borrower can show the ability to cash flow and is not overextended.
- Risk ratings are critical
- Credit Administration: Final Interagency Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts – Joint Agency Release 6-29-23
- Underwriting Conditions will tighten.



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