

Blog Post

The Line Reports from the MBA Servicing Conference: Multifamily Servicers Report Increased Watchlist Loans, Prepare for Wave of Maturing Loans

Posted on **May 27, 2010** by Peter K. McKee, Jr.

Panelists from Fannie Mae, Freddie Mac, Wells Fargo and M&T Realty Capital concurred that, with fewer refinancing options available to borrowers near-term, maturity defaults pose a looming problem that will initially spike in 2013. The number of stressed loans is mounting as well, pushing more loans to watchlist status and requiring greater servicer resources.

Wells Fargo has added staff and is using technology to leverage resources, but it is burdened by a dizzying number of compliance and audit requests, both internal and external.

Freddie Mac reported on the results of its requiring broader and deeper quarterly information from its correspondent servicers. The exercise has allowed Freddie to better differentiate its loans into risk buckets, and enabled it to calibrate its loan loss reserves.

In response to questions about trends in property condition, Freddie reported it had promulgated inspection best practices, but had not yet validated their effects in the field. It was also checking on deferred replacement reserves for its loans, noting that it was important to "act before the death spiral began."

Fannie Mae has begun requiring quarterly information as well. Based on effective gross income and occupancy information provided by its primary servicers, it loads expenses to arrive at DSCRs. Fannie is also adapting its inspection form to move from the more subjective MBA template to something with more readily sortable data. More attention is also being directed at building or other code violations, especially in New York City, since that can often be a leading indicator of deterioration to come. (As an aside, see my earlier post "Must Investors Rush In ..." for a vivid example of just such a situation.) Last, Fannie is looking at its middle tier borrowers (\$50-\$250 million), including their non-Fannie debt, to analyze that group's future ability to perform.

All the panelists expressed a sense that borrowers were reluctant to face the possibility that the market recovery might be either too tepid or late to bail out their project, and that delays in confronting that could prove their undoing.

Returning to the panel's main themes, Wells Fargo's representative pointed out that one-third of its portfolio matures in the next 5 years, and that grappling with that was a critical institutional challenge. Trends in delinquencies, defaults and loss severities was also palpable: loss severities of 7% in 2007, 11% in 2008, and over 30% in 2009. The good news? There were no surprises in this data, most of it being traceable to the 2006-07 origination cycle when interest-only loans and relaxed underwriting predominated.

Asked whether owners were observably bleeding their properties, Fannie Mae's panelist commented that she'd noticed borrowers would bleed their CMBS properties first for fear of being tainted by Fannie going forward. A recognition of the GSE's market dominance, to be sure. Still, Fannie has been looking at how these borrowers have been handling non-DUS loans because this information predicts their likelihood of bleeding Fannie properties, too.

Overall impressions from this panel? Servicers have ample reason to be concerned, though they are not deluded by the scale of the problems or resources required. Clearly borrowers should be better prepared for negative contingencies than they appear to be now.

So it's a "hope for the best, prepare for the worst" scenario.