

Performance of Commercial and Multifamily Mortgages Remains Stronger than Overall Bank/Thrift Loan Portfolios

Commercial and multifamily mortgages have been the topic of a great deal of discussion and conjecture in recent months. In March 2009, MBA published a DataNote analyzing bank data as of the fourth quarter of 2008. That DataNote found that commercial and multifamily mortgages were among the best performing loans held by banks and thrifts. This DataNote updates the analysis with data as of the fourth quarter of 2009 and finds that commercial and multifamily mortgages continue to have the lowest charge-off rates of any loan type at banks and thrifts and perform better than the overall portfolio of loans and leases held by these institutions.

BACKGROUND

Commercial banks and thrifts invest in and hold a variety of assets to earn income on the money raised through checking accounts, savings accounts, certificates of deposits, bank debt and other liabilities they hold. A key component of these assets, 56 percent at the end of 2009, is loans and leases — including 1–4 family residential mortgages, home equity loans, credit cards, non credit card consumer loans, commercial mortgages, multifamily mortgages, construction loans and commercial and industrial loans.

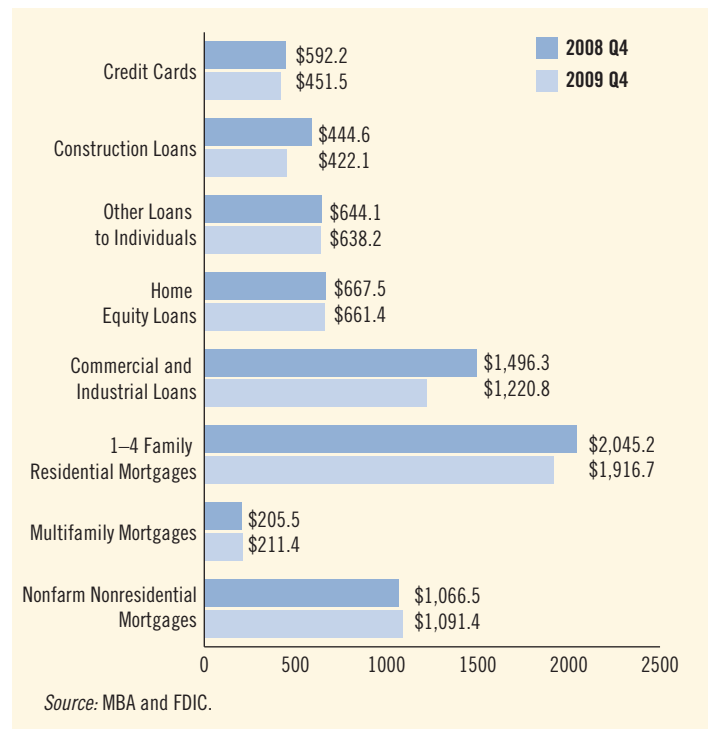
LOAN HOLDINGS

Of the various types of loans and leases, 1–4 family residential loans make up the largest share of banks' loan holdings (\$1.9 trillion or 26 percent of the total), followed by commercial and industrial loans (\$1.2 trillion or 17 percent of the total) and commercial mortgages (\$1.1 trillion or 15 percent of the total).¹ At \$211 billion, multifamily mortgages account for three percent of bank-held loans and leases. Over the course of the last year — in the face of the recession, the credit crunch and headlines about the lack of capital available for commercial real estate — commercial and multifamily mortgages are the only category of bank loan to have seen growth (see Figure 1).

LOAN PERFORMANCE

Looking across the various loans and leases held by banks and thrifts, commercial and multifamily mortgages finished 2009 with 30+ day

FIGURE 1: BANKS & THRIFTS: BALANCE OF LOANS HELD BY BANKS AND THRIFTS (\$BILLIONS)

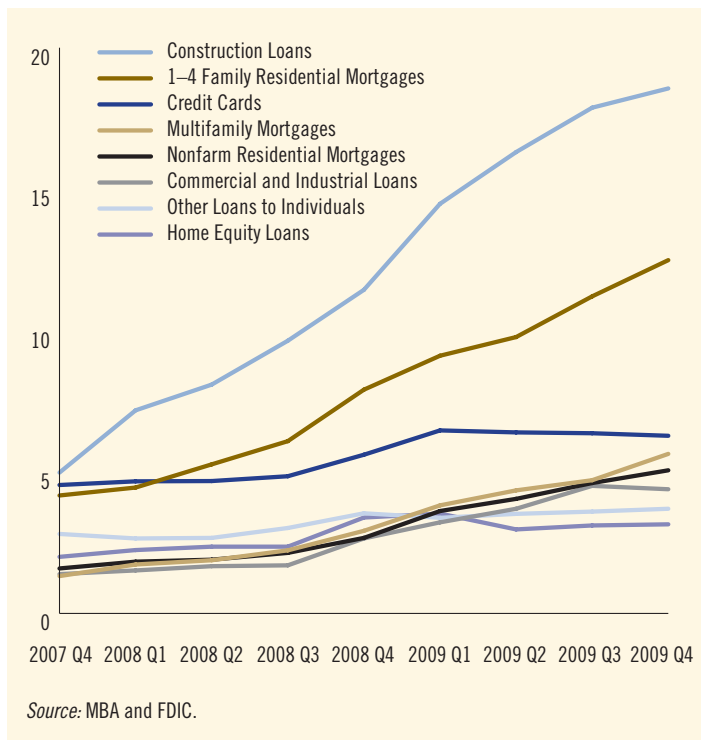


delinquency rates lower than the average for all loans and leases held by banks and thrifts. At the end of the fourth quarter, 7.30 percent of the balance of all bank and thrift loans were 30 or more days past due. Commercial mortgages had a 30+ day delinquency rate of just 5.06 percent and multifamily mortgages recorded a rate

of 5.64 percent. Construction loans, driven by poor performance among single-family-related land and construction loans — had the highest delinquency rate, at 18.56 percent. Single-family mortgages had the second highest rate, at 12.49 percent. Credit cards saw the third worst delinquency rates, at 6.28 percent. Commercial and industrial loans saw delinquency rates of 4.39 percent, slightly lower than commercial mortgages. Home equity loans recorded a 30+ day delinquency rate of 3.15 percent and 3.70 percent of the balance of other loans to individuals were delinquent (see Figure 2).

As with many other types of loans, commercial and multifamily mortgages continued to see increases in loan delinquencies during the fourth quarter. At the end of 2009, delinquency rates on commercial mortgages and multifamily mortgages were 0.5 and 0.9 percentage points higher than they had been at the end of the third quarter, respectively. This compares to a 0.44 percent rise for all loans and leases. Among other types of loans, 30+ day delinquency rates on single-family mortgages increased by 1.3 percentage points, delinquencies on construction loans increased by 0.7 percentage points and home equity loans remained essentially unchanged. Credit card loans and commercial and industrial loans each saw a 0.1 percent decline in delinquencies.

FIGURE 2: BANKS & THRIFTS: 30+ DAY DELINQUENCY RATES OF LOANS AND LEASES (PERCENT)



CHARGE-OFFS

As banks and thrifts recognize troubled loans as uncollectible, they charge them off — removing the uncollectible loan balances from their balance sheets and recognizing the losses in their income statements. While delinquency rates represent the share of loans that are not paying on time, charge-off rates represent a bank’s assessment of the share of the outstanding loan balance they are unlikely to get back.

Commercial and multifamily mortgages provide security to their lenders in that a) even when under stress the commercial property continues to provide some level of income to help pay its debt service, except in the most extreme situations, and b) for every loan there is a real, tangible asset pledged as collateral should the loan become delinquent. For these reasons, commercial and multifamily mortgages have historically not experienced the same rate of losses as most other types of loans. This is evident in the charge-off rates experienced by banks and thrifts.

Over the course of 2009, commercial and multifamily mortgages had the lowest charge-off rates of any loan type at commercial banks and thrifts. In 2009, banks and thrifts charged off 0.8 percent of their balance of commercial mortgages and 1.1 percent of their multifamily mortgages. By contrast they charged off 1.7 percent of their balance of 1–4 family residential loans, 2.4 percent of their commercial and industrial loans, 2.9 percent of their home equity loans, 3.0 percent of their non credit card consumer loans, 5.4 percent of their construction loans and 9.1 percent of their credit card loans. The charge-off rate for commercial mortgages was less than half that of single-family mortgages, the next lowest group, and less than one-tenth of the rate for credit cards, the loan type with the highest charge-off rate (see Figure 3).

In aggregate dollars, the charge-offs of commercial and multifamily mortgages by banks/thrifts also remain very low in relative terms. Over the course of 2008 and 2009, banks and thrifts have charged off more than \$105.5 billion in loans to individuals, \$83 billion in residential mortgages, \$51 billion in commercial and industrial loans and \$47 billion in construction loans. By contrast, over the same period they have had to charge-off only \$11 billion of commercial mortgages and \$3 billion of multifamily mortgages.

Had banks and thrifts not lent on commercial and multifamily mortgages, and instead lent that money through other loan types, they would have seen roughly \$36 billion in charge-offs and losses in 2008 and 2009 that they have not seen.

FIGURE 3: BANKS & THRIFTS: CHARGE-OFF RATES OF LOANS AND LEASES

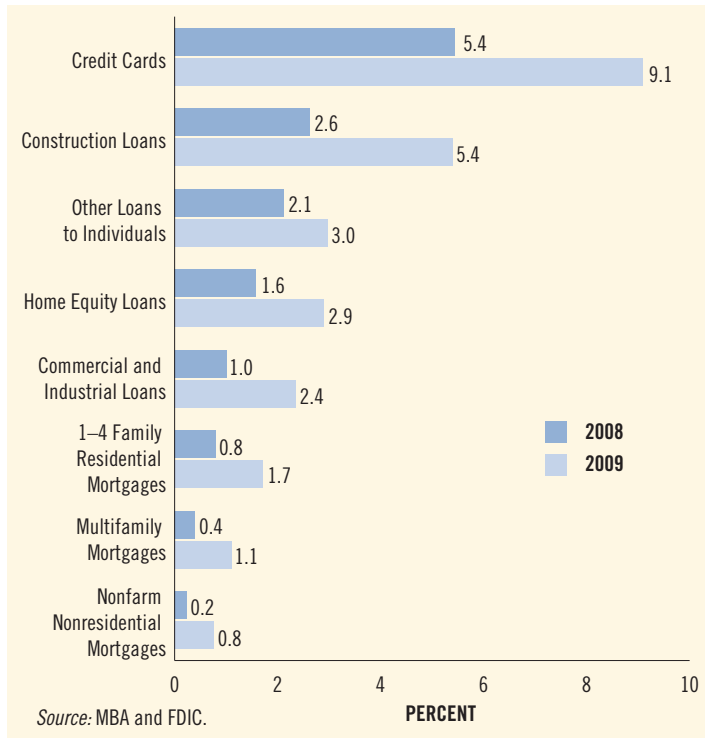
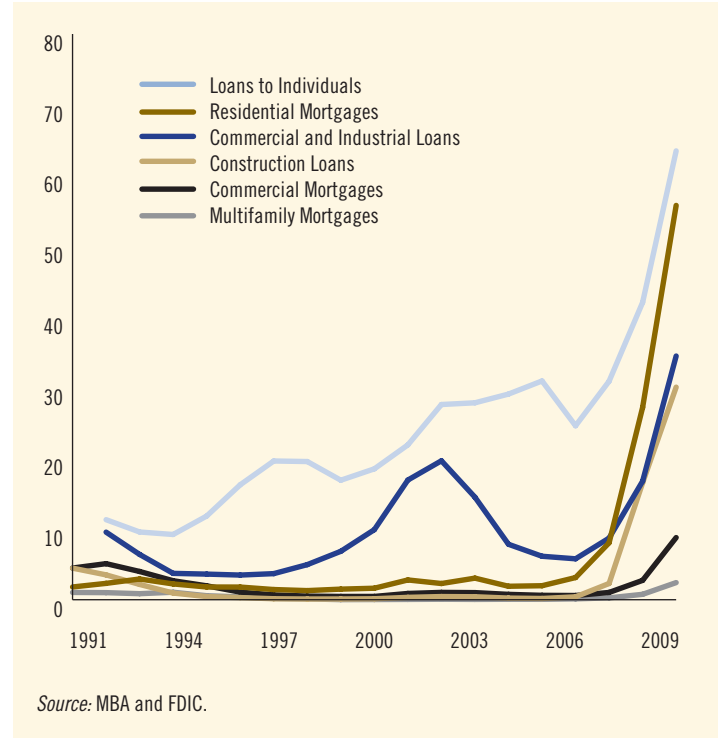


FIGURE 4: CHARGE-OFFS AT BANKS AND THRIFTS (\$BILLIONS)



CONCLUSION

As noted in the 2008 DataNote, commercial and multifamily mortgages are an important part of the holdings of commercial banks and thrifts. Like other parts of the economy, the performance of commercial and multifamily mortgages has been negatively impacted by job losses, consumer restraint and manufacturing declines. The relatively stable performance and low charge-offs of commercial mortgages through the recent recession, however, have helped, rather than hurt, the stability of banks and thrifts.

NOTE

1. It is important to note that of the \$1 trillion of commercial mortgages held by banks, roughly 45 percent are business loans backed by an owner-occupied property. These are not what one typically thinks of as commercial property mortgages — mortgages made to income-producing properties such as office buildings, shopping malls or warehouses, in which the loan will be repaid by rents paid by tenants. Rather these are loans to other types of businesses, paid back by those businesses' incomes, but with real property owned by the businesses pledged as collateral. Of the \$1.5 trillion of bank loans cited by the Federal Reserve as relating to the commercial and multifamily real estate market, only about \$776 billion relates to the market for income-producing office, retail, apartment, and other commercial properties. In addition to the owner-occupied

properties, the Federal Reserve's \$1.5 trillion mortgage debt outstanding estimate from the Flow of Funds Account includes a portion of banks' construction loans, including single-family construction lending.

About Research DataNotes

Author:

Jamie Woodwell, Vice President of Commercial Real Estate Research, Mortgage Bankers Association

Any questions or for more information, please contact Jamie at jwoodwell@mortgagebankers.org.

Research DataNotes are a series produced by members of MBA's research and economics group designed to explain and explore technical aspects of the real estate finance industry.

© 2010 Mortgage Bankers Association, Washington, D.C. All rights reserved.

All rights reserved. No part of this publication may be downloaded, stored in a retrieval system, reproduced or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without the prior written permission of the copyright owner.

Disclaimer: Although the MBA takes great care in producing DataNotes and all related data and other information products, MBA does not guarantee that the information provided is accurate, current or suitable for any particular purpose. MBA Research DataNotes is provided on an "as is" basis, with no warranties of any kind whatsoever, either express or implied, including, but not limited to, any warranties of title or accuracy or any implied warranties of merchantability or fitness for a particular purpose. Use of the information provided in MBA Research DataNotes is at the user's sole risk. In no event will MBA be liable for any damages whatsoever arising out of or related to the information provided, including, but not limited to direct, indirect, incidental, special, consequential or punitive damages, whether under a contract, tort or any other theory of liability, even if MBA is aware of the possibility of such damages.