Where the Bank CRE Loans Are Going

Commercial mortgage originations ‘fell dramatically’ in Q3 compared to pre-Covid times.

By Erik Sherman

At this point, many people have a pretty good idea that banks are facing significant challenges from CRE loans — even federal regulators. The Financial Stability Oversight Council recently released its annual report that both said, “Despite the regional bank stress in the Spring, the U.S. banking system remains resilient overall” and noted that commercial real estate loans, are a significant potential vulnerability.

The FSOC noted that CRE loans are “the largest loan category among almost one-half of U.S. banks” and that a quarter of banks “have CRE loan portfolios that are large relative to the capital they hold.”

And so, the state of CRE loans is important. It could affect bank stability and ability to lend, and also undermine the value of CRE property.

The title of a new Trepp report on bank CRE loan performance gives a sense of where things are going: Bank CRE Loan Performance Q3 2023: Office Sector Sees Continued Surge in Charge-Offs and Delinquencies, Paired with Steep Declines in Occupancy and Originations. It’s not all bad news, just a lot.

“Commercial mortgage origination volumes for bank-held commercial real estate (CRE) loans fell dramatically in the third quarter, with the office sector showing the lowest origination volume in Q3 relative to the pre-Covid 2019 average quarterly origination volume for the sector,” they said. “Furthermore, the mortgage underwriting terms for any new originations in the third quarter show greater weakness relative to originations made in prior quarters. In terms of bank loan performance, net charge-offs, delinquency, and occupancy rates all largely reflect more stress in CRE lending, with the office sector driving most of the negative changes.”

The analysis was done through an examination of trends in Trepp’s Anonymized Loan-Level Repository (T-ALLR) data set, which is “a diverse set of loans totaling about $160 billion sourced from multiple banks.”

New CRE loan originations in Q3 were $2.5 billion, down from $4.7 billion in Q2. Multifamily (from $2.2 billion to $1.1 billion between quarters) and lodging ($0.2 billion down to $0.1 billion) saw the biggest quarter-over-quarter decreases.

Compare the 2023 Q3 origination to the average quarterly origination in 2019 — as a pre-pandemic baseline — and office loan origination had the biggest falloff, being only 24% of previous.

“A bright spot is that industrial loan origination volumes didn’t decrease nearly as much from Q2 to Q3 2023 as the other property types did,” they wrote. “All other property types saw origination volumes that fell around 40% or more, whereas the origination volume for the industrial sector only saw a 3.2% decrease to $261 million in Q3 from $270 million in Q2.”