WHOLE LOAN TRADING ACTIVITY

Hospitality loan sales have dominated an anemic whole loan trading market since the onset of COVID-19 and ensuing collapse of the lodging market for a number of reasons:

- Far worse and more abrupt revenue impact relative to prior crises (Zika, Financial Crisis, Russia Crisis) / inability to model recovery timeline
- Anticipated government stimulus which never materialized like the HOPE Act of 2020(1) which was to provide preferred equity capital for re-opening / operations beyond de minimis PPP / EIDL lending
- Willingness of banks and other lenders to offer deferral/forbearance agreements, including CARES Act 4013 deferrals

During 2Q20 and 3Q20, transitional assets and construction loans remained difficult to monetize and were trading with limited frequency due to bid-ask spreads stemming from COVID-related uncertainty. In 3Q20 and into 4Q20, whole loan trades began clearing for performing / nonperforming loan sales for which borrowers have requested and / or received pandemic related debt relief. In 1Q21, a jolt in liquidity in the securitized product market, bolstered by government bond market interventions, supported CLO and CMBS bond pricing and drove a resurgence in liquidity in all whole loan markets.

Mission Capital's Transaction Tracker of hospitality-specific loan sales indicated the following activity and success rates for all of 2020 as of 12/2020:

	Sale Count	Unpaid Principal Balance	Sell Through % / Success Rate	Pull Through UPB
COVID-era 1H2020	16	$954,857,228	14%	$131,152,500
COVID-era 2H2020 / Pending	15	$1,490,902,402	29%	$426,500,000

Notably, measuring hospitality loan trading activity from the beginning of 2020 through May 2021 shows that certain delayed / negotiated transactions were completed (including delayed 4Q20 transactions) and many other loan sales traded. Loan sale activity and Sell Through % have dramatically increased and suggests an accelerating marketplace going into 2H2021. Trailing 18-month trading results are as follows:

	Sale Count	Unpaid Principal Balance	Sell Through % / Success Rate	Pull Through UPB
COVID-era 1H2020	16	$954,857,228	14%	$131,152,500
COVID-era 2H2020 to 6/30/21	31	$3,211,138,402	58%	$1,873,847,520

Prevailing pricing for normally distributed performance portfolios (elevated LTV, sub-performing, COVID re-performing, performing) has risen from 75% - 80% of UPB to 90% - 95% of UPB from 3Q2020 to 2Q2021.

WHOLE LOAN TRADING ACTIVITY

Additional whole loan trading catalysts and observations for 2021 include:

- **Strengthening bank balance sheets**, due to a somewhat unexpected recovery in the investment sales market will provided financial latitude for banks to accept discounts on the limited remaining problem hot spots such as legacy hospitality, retail and senior care loans.
- **Office assets are starting to present as problematic** and will increasingly be the focus of loan sales in 2H21 due to the lackluster re-occupying.
- Sales of COVID and pre-COVID issue loans will have muted bank stock price effects due to already expected losses, bank stock performance and increasing M&A activity driven by rising stock prices.
- **Demand for seasoned performing loans of all types** increasing due to excess liquidity / excess deposits, part arising from unspent and still unforgiven PPP funds.
- Strong demand for single family loans and the rise in single family property values has spurred legacy whole loan trading the GNMA Early Buy Out (EBO) transactions at aggressive pricing.
- Continued anxiety regarding impending tax increases, reduction in 1031 allowed transactions, increases in capital gains taxes and other American Families Plan changes are driving transactions and payoffs of otherwise marginal loans.

Notwithstanding the June 2021 three month eviction moratorium extension by the Agencies, bank regulators will begin to increase pressure on CARES Act 4013-designated loans to either return the line or be classified as a TDR. January 2022 is reportedly the drop dead target date for these deferred payment loans to be properly classified.

Banks invested substantial time and resources to evaluate troubled loans during 3Q20 and 4Q20 to identify / separate long term credit / collateral issue loans from recovering / borrower supported loan relationships. The expectation is that the longer term issue loans will be most likely to be offered in the secondary market in 2H 2021 but brisk resolution activity is reducing this exposure.

Bank analysts note that Section 4013 of the CARES Act entitled "Temporary Relief from Troubled Debt Restructurings has provided wide latitude to banks in avoiding migration of Substandard or Special Mention loans to TDR status based on deferrals / forbearances.

Mission Capital continues to monitor secondary market transactions as well as industry sources for insight into the effect the regulations will have on the value of collateral / loans longer term.

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