COVID-19 And Your CRE Portfolio

business customers pandemic CRE

Summary: Keeping investments together these days isn't easy for your CRE borrowers. Top three things to do to protect your CRE loan portfolio.

We found out Lego has an underground vault with 500 iconic sets for viewing. What a cool way to keep them all together! Similarly, many commercial real estate (CRE) borrowers are trying to keep their investments together these days.

It is not easy for your CRE customers given the current COVID-19 and economic situation. Certain businesses are doing better than others; generally, grocery stores are still busy, while restaurants have taken a big hit. As you know, it is important to know how your business customers are doing, especially your CRE borrowers.

According to the Trepp Bank Research (March report), the cumulative default rate across all commercial mortgages will increase to 8%, which is a drastic uptick from the current 0.4% default rate. The scenario used for this forecast is an adapted form of the bank regulators' Severely Adverse scenario, with changes to address the more major expected drops in the lodging (34.8%) and retail industries (16.0%). Office, multifamily and industrial have 4.3%, 3.3%, and 3.0% projected default rates, respectively. As the default range by industry is quite vast, it is important to know your loans by industry and area and to get information regularly from your borrowers.

1. **Review your loan portfolio by industry (and geographic area, if relevant).** This will allow you to focus on the areas most severely hit during the crisis. Where you have losses in some areas, you may find gains in other areas. Warehouses, transportation, and logistics are all still needed. Do you have some of these in your portfolio? What about smaller businesses? Are they able to stay afloat with pickup orders and delivery or virtual services such as tutoring, exercise classes, etc.? Sorting your CRE portfolio into more granular slices may help you assess risk rating and/or loan loss reserve adjustments.
2. **Get frequent updates.** Are your CRE borrowers providing you with frequent updates, showing they are transparent about their situation? Ask them for specific information that you need on a regular basis along with how detailed you need it, so they know what you are expecting. Are their tenants asking for concessions or rent deferrals? Do they have a game plan? How are the risks being addressed from a short term and long term perspective? What is the COVID-19 policy and how is it addressing cash flow with social distancing, payments with government stimulus options for their businesses, etc.
3. **Prepare for the re-opening of the economy.** The economy will eventually open up again, but it won't be the same for every business. Some areas are opening earlier than others and will more easily be able to rehire employees and/or get back to onsite working vs. working remotely. How are the property managers handling maintenance and inspections safely? Are move-in timelines still reasonable? When people move back, will everything be ready? Will further loan modifications be needed before people get back to work?

While we know you are working hard on all of this, it never hurts with some quick reminders.

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Now more than ever, it is important to stress test loans of all types from multiple perspectives and on a portfolio basis. Get expert help to save you time and money. Learn more about credit stress testing today.