March 23, 2020

Via electronic submission – www.regulations.gov

The Honorable Jerome H. Powell
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave NW
Washington, DC 20551

The Honorable Steven T. Mnuchin
Secretary
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

The Honorable John C. Williams
President and Chief Executive Officer
Federal Reserve Bank of New York
33 Liberty Street
New York, NY 10045

The Honorable Mark A. Calabria
Director
Federal Housing Finance Agency
400 7th Street, SW
Washington, DC 20219

RE: Request for Immediate Support of Mortgage Markets

Dear Sirs:

The Commercial Real Estate Finance Council (CREFC) recognizes that the Federal Reserve System took immediate and extreme steps to shore up confidence and the stability of the financial system as soon as events related to COVID-19 began transmitted to the markets and the economy. Notwithstanding these actions, CREFC is requesting immediate and extensive support of the commercial and multifamily agency and private-label mortgage markets. The current extreme funding pressures on a wide range of financial institutions and a significant contraction in available liquidity at this time present a systemic risk to the U.S. mortgage markets, the financial system, and the economy as a whole.

Many of CREFC’s members view the damage that has been caused already to the commercial and multifamily real estate markets (and will continue to do so without decisive action) as much broader, deeper, and faster moving than the crisis in 2008. As of now, the freezing up of the U.S. capital markets caused by COVID-19 has wrought more damage in a handful of weeks than was seen over several months in 2008. With that in mind, we anticipate this request to be the first in a sequence that we believe will be necessary (but most urgent in the short term) as we continue to monitor and assess the situation.

CREFC’s members (340 companies) represent U.S. commercial and multifamily real estate investors, lenders, and service providers – a market valued at an estimated $6.3 trillion supported by $4.4 trillion of commercial real estate (CRE) debt. Commercial banking organizations, insurance companies, Agency mortgage-backed securities (Agency MBS), commercial mortgage-backed securities (CMBS), and other lenders are the core sources of financings for commercial and multifamily real estate.
We ask that you act in the immediate term to implement the following measures in order to avoid the negative loop created by a liquidity crisis that has the real potential of sharply reducing the continued flow of capital to commercial and multifamily real estate.

1. Re-establish the 2008 Term Asset-Backed Loan Facility (TALF) to prevent a worsening economic/capital-markets crisis as we battle an unprecedented medical one. TALF 2.0 would provide investors with non-recourse loans secured by new-issue and legacy mortgage-related securities, including but not limited to agency and private-label single-family and multifamily securities, private-label Commercial Mortgage Backed Securities (CMBS), and specific types of high-grade credit risk, such as the GSE’s credit risk transfer securities. A reinstatement and refinement of TALF are of the utmost importance and should be instituted as soon as possible to stave off further deterioration of these markets and further reduced liquidity to vital sectors of the U.S. economy.

Given the generally longer-term loans collateralizing commercial and multifamily real estate securities, as in TALF 1.0, we would advise maintaining the maximum TALF loan five-year maturity. Moreover, TALF 2.0 haircuts should be reduced relative to those that prevailed for TALF 1.0, and should range between 5% and 10%. There are a number of reasons for the reduced haircuts, including:

- More conservative credit criteria applied to commercial and multifamily loans over the last ten years, and
- Significantly higher credit-enhancement levels required by credit rating agencies post crisis.

In addition, eligibility criteria in TALF 2.0 should require that collateral have an investment-grade rating from one or more of the nationally recognized statistical rating agencies (NRSROs). Again, while TALF 1.0 addressed the most senior bonds in the capital stack only, today’s more conservative underwriting and heightened credit enhancement should allow for an expansion of eligible transactions to all investment-grade.

2. Raise the commitment to the System Open Market Account (SOMA) to purchase more Agency MBS, and extend those purchases to include Agency multifamily MBS/CMBS.

3. CREFC’s members also see value in lifting the government-sponsored enterprises’ (GSEs) portfolio caps temporarily, which would allow them to use their retained portfolios to purchase MBS with a focus on specified pools. It is the specified pool market sector that is experiencing some of the most acute deterioration in liquidity. Market valuations for these pools have dropped substantially, leading to significant margin calls and further asset price declines. As in other sectors, the specified pool price declines are not the result of poor underlying asset quality or performance, but the lack of liquidity. Currently, the Fed’s operations are only focused on TBAs as the Fed does not have the operational capabilities to purchase specified pools. The sooner action is taken, markets will be able to support price discovery far more quickly.

We recommend these steps in light of the accelerated market deterioration occurring at this time. Without these or similar measures, we believe that non-bank financial institutions will suffer significantly, resulting in strain on the mortgage and fixed income markets and the economy broadly.
Prior to the start of COVID-19, non-bank lending institutions were considered to be in healthy financial condition. Since the crisis began, their collective share price has dropped sharply, indicating the severity of the liquidity contraction and the extremity of the environment in which they are forced to fund and revalue their portfolios.

As part of these liquidations, these entities will be forced to sell assets under “fire sale” conditions into a market where there are few buyers, which will further depress the value of mortgage-related securities.

Such a fire sale is likely to have knock-on effects for insurance companies, asset managers, and other holders of mortgage-debt.

Banks, which extend financing to investor-focused credit funds and mortgage REITs, may need to make margin calls in order to adhere to their own liquidity requirements, which can cause further deterioration in asset values and pressuring of liquidity.

Mortgage rates in the marketplace will undoubtedly continue to rise. Today the spread between Treasuries and mortgages is as wide as it was in 2008 and could widen still.

CREFC asks that the Federal Reserve, Treasury, and Federal Housing Finance Agency continue to take decisive steps to reestablish liquidity in the single family, multifamily, and commercial mortgage markets to stabilize asset prices and shore up the balance sheets of non-bank market participants’ balance sheets. We stand ready to provide additional input and are eager to assist in facilitating a response as you deem necessary.

Sincerely,

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cc:
Lorie Logan
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