CMBS Credit Focus

Securitized Mezz: Workout Dynamics in Public Display

Takeaways from Rosslyn Office Portfolio and Other Securitized Mezz Deals

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The situation at the $803.5 million Rosslyn Office Portfolio (GSMS 2021-ROSS and GSMS 2021-RSMZ) could provide the market a blueprint of how servicers work out complex capital structures on troubled office loans. We believe more clarity on loan resolutions is critical to alleviate the headline risk in the office space, and perhaps re-engage investors currently sitting on the sidelines. Rosslyn could feature the workout dynamics of a senior mortgage and mezz loan in public view.

The $112.5 million GSMS 2021-RSMZ is secured by a mezz position on the 2.1 million sf seven-property office portfolio in Arlington, VA (Figure 1). As such, the RSMZ deal disclosures could report information that is typically not available on non-securitized mezz positions sitting below securitized senior debt.[1] Notably, the Rosslyn mezz loan transferred to special servicing in May 2023, ahead of its maturity, according to servicer commentary. The borrower stated that they did not expect to refinance or extend the loan. In turn, the $691 million senior mortgage behind GSMS 2021-ROSS also transferred to special servicing in late May. This followed earlier servicer commentary that curiously noted the mortgage borrower will seek refinancing, as Morningstar flagged at the time.

Figure 1. Rosslyn Office Portfolio Loan and Property Parameters

Securitized Asset Type	Senior Mortgage Loan	Mezzanine Loan
Deal	GSMS 2021-ROSS	GSMS 2021-RSMZ
Balance	$691,000,000	$112,500,000
Maturity	June 2023	June 2023
Coupon	1ML + 2.92%	1ML + 9.50%
Loan Status	Matured Non-Performing	Matured Non-Performing
DSCR	0.94x	0.72x
LTV	61.9%	71.9%
Appraised Value	$1,117,100,000 (as of Feb 2021)	
Property Type	Office	
Property Size	2,127,843 square feet (across 7 buildings)	
Occupancy	78% as of 3/31/2023	
Location	Arlington, VA	

← June 2023 is the initial maturity. Borrower had three 1-year extension options (through 2026) but does not currently meet all conditions necessary to exercise such option

Source: MCIA and Academy Securities

1 "Mezz Loan Sales: A Potential Headache for CMBS Workouts," CMBS Credit Focus, Academy Securities, March 22, 2023

Contractual Provisions and Mezz Paydowns Directly Impact Mortgage Path

Rosslyn underscores a few notable aspects on the relationships between senior and mezzanine debt, and the implications for workouts amid the stress across CMBS properties:

- **Mortgage extension mezz dependency.** Servicer commentary suggests that the Rosslyn mortgage borrower does not plan to exercise the loan's contractual extension option because it was not able to secure refinancing of the mezz loan. Refinancing (or extension) of the mezz loan is one of the conditions for extending the mortgage. This shows the challenges CMBS loan workouts may face purely based on mezz-related contractual provisions (separate from any adversarial actions mezz lenders can take). The $510.5 million BX 2018-GW (Grand Wailea) and the $281 million BX Trust 2018-BILT (Arizona Biltmore) are two other examples of CMBS deals with securitized mezz positions that require extension or repayment of the mezz loan to exercise contractual extension option on the mortgage loan.

Figure 2. Outstanding Securitized Mezz Transactions

Loan Name	Mezz Deal	Orig Bal ($000'S)	Cur Bal ($000'S)	Property Type	Related Senior Deal
Arizona Biltmore	BX 2018-BTMZ	37,000.0	37,000.0	Hotel	BX 2018-BILT
Grand Wailea	BX 2018-GWMZ	66,000.0	66,000.0	Hotel	BX 2018-GW
Palmer House Hilton	JPMCC 2018-PHMZ	89,585.0	89,585.0	Hotel	JPMCC 2018-PHH
Atlantis Paradise Island	BHMS 2018-MZB	213,750.0	213,750.0	Hotel	BHMS 2018-ATLS
Stonemont NNN-Leased Portfolio	JPMCC 2020-NNNZ	77,750.0	260.1	Triple-Net	JPMCC 2020-NNN
Rosslyn Office Portfolio	GSMS 2021-RSMZ	106,875.0	106,875.0	Office	GSMS 2021-ROSS
NYC Affordable Housing Portfolio	JPMCC 2021-NYMZ	89,015.0	89,015.0	Multifamily	JPMCC 2021-NYAH

Source: MCIA and Academy Securities

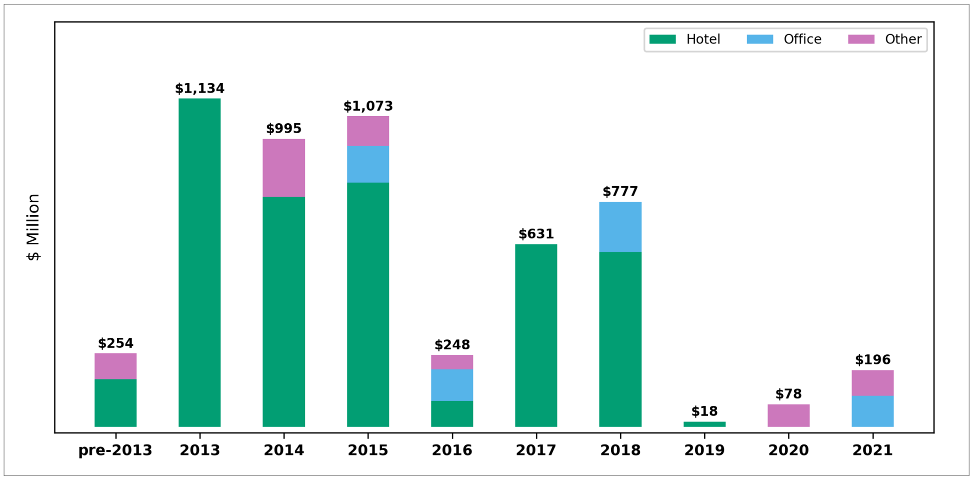
- **Mezz paydowns can precede the mortgage.** Deal documents and paid off securitized mezz deals make it clear that borrowers can pay down mezzanine loans ahead of any senior mortgage payoff, even in distress situations. Examples include JPMCC 2020-NNNZ, which nearly paid off its $81.9 million mezzanine loan on the Stonemont Portfolio. The mortgage on the portfolio of 44 single-tenant, triple-net properties is still outstanding in JPMCC 2020-NNN. In turn, BHMS 2018-MZC paid off its $100 million original balance tied to one of three mezzanine positions on Atlantis Paradise Island Resort. The mortgage on the Bahamas resort backs the $1.2 billion BHMS 2018-ATLS. Another $225 million mezz note on the property is securitized and outstanding in BHMS 2018-MZB. Early mezz payoffs may appear counter-intuitive amid basic seniority standards that give preference to senior payments. Still, senior loans generally permit such mezz payoffs, which de-lever the debt load and would be a credit positive for the mortgage. Interestingly, investors in the subordinate tranches of the mortgage-backed deals may be less receptive to early mezz loan paydowns. As borrower payoff options potentially dwindle amid poor property performance, subordinate bond interest may stand in direct conflict that of the mezz lender.

- **Property releases tied to mezz payment.** Deal provisions may allow borrowers to release properties across portfolio loans only after some prepayment on an outstanding mezzanine loan. One example is the Stonemont Portfolio we flagged above. The borrower released 22 properties since issuance, after meeting the mezz repayment condition in the deal. Generally, when a mezz loan is securitized, investors may be able to easily track its repayment. Mezz-driven condition for property releases could serve as a strong incentive to pay down mezz loans. Borrowers may increasingly look to release properties amid performance divergence across portfolios, as we recently discussed in detail.[2] The mezz condition joins other notable release provisions such as dynamic release prices, and property-specific prices.

Securitized Mezz Issuance Recently Dwindled, but is Resurgence on the Horizon?

Securitized mezz issuance saw elevated levels in 2013 through 2018, mostly on hotel loans (Figure 3). Issuance sharply dropped starting in 2019, recording only $196 million in 2021. Many of the securitized mezz deals have paid off. But several notable mezz deals remain outstanding, as we showed in Figure 2. It remains to be seen if originators would resume securitizing mezz loans. Our general view, consistent with market participant commentary, is expecting to see a surge in mezz lending originations, amid pullback by senior lenders and rising demand for property recapitalizations.[3] Anecdotally, the number of shops providing subordinate debt on CRE properties rose to 163 from 152 a year ago, according to CMA's recent annual survey.

Figure 3. Securitized Mezz Issuance by Property Type



Source: Bloomberg and Academy Securities

2 "Release Prices: Cherry Picking Across Office Portfolios, Sometimes at a Discount," CMBS Credit Focus, Academy Securities, April 13, 2023
3 "Office Modifications: 285 Madison Could Offer a Blueprint for More to Come," CMBS Credit Focus, Academy Securities, October 27, 2022

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