



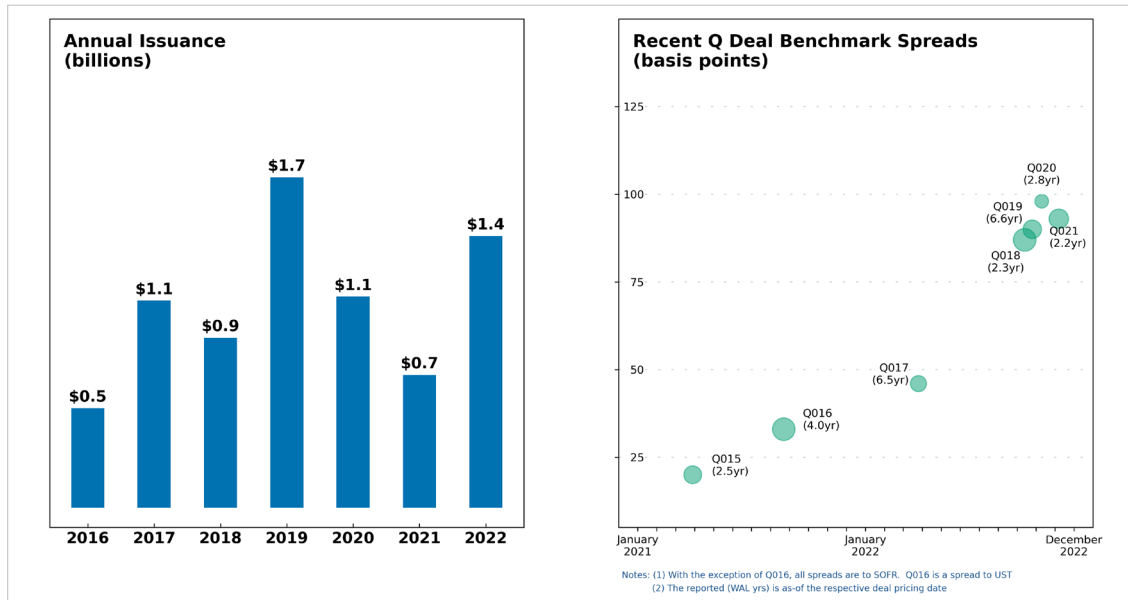
Value Considerations as Q Deals Absorb Transitional Collateral

The migration of transitional multifamily loans away from the dormant CRE CLO market offers investors a window of opportunity to gain exposure to the collateral with different deal structure and risk profile. In particular, Freddie Mac’s Q-Deals have been absorbing some of the CRE CLO issuers originations. Issuance has markedly ticked up towards the end of 2022, reaching an overall volume of \$1.39 billion (Figure 1). Four deals priced just during Q4 2022, with benchmark class spreads ranging from 87bp to 98bp.

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Figure 1. Q-Deal Issuance and Spreads, 2016-2022



Source: Freddie Mac and Academy Securities

Divergent Prepay Provisions Poised to be Impactful

The Freddie execution offers guaranteed classes amid a potential softening of the multifamily sector.¹ The recent troubles of large multifamily loans such as MFP Portfolio (\$382.5 million, JPMCC 2019-MFP) and Parkhill City (\$225 million, PKHL 2021-MF), while not in GSE deals, still spotlighted growing fractures in a CRE sector that has been very resilient so far. In turn, Q deals

¹ “Manufactured Housing: Resilient Segment Amid Potential Multifamily Softness,” Securitized Products Special Topics, Academy Securities, July 27, 2022

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also feature a fairly wide variation of prepayment restrictions. For example, in FHMS Q-018 most loans have a yield maintenance prepayment provision (or 1%, whichever is greater) that typically runs for 15 months, followed by an open period (Figure 2). In Q-017 most loans are in a lockout period for nearly a year, and then have a long 1% prepay provision. Lastly, in Q-015 there are no prepayment restrictions, according to deal documents.

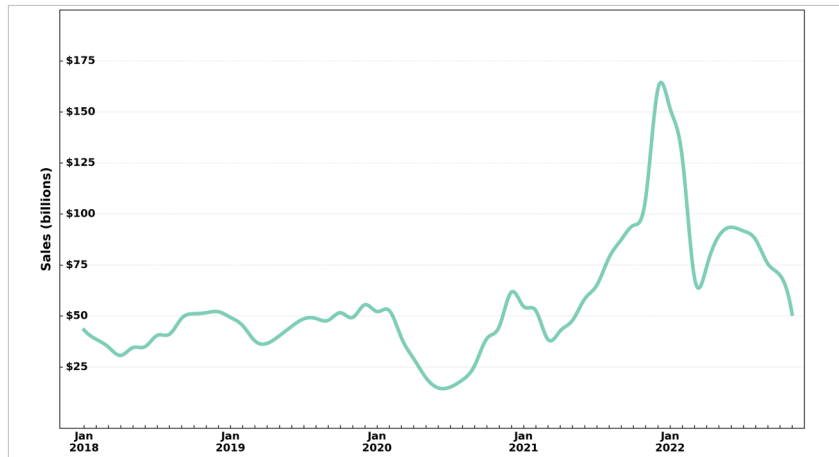
Figure 2. 2022-vintage Q-Deal Pool Characteristics

Deal	Q-017	Q-018	Q-019	Q-020	Q-021
Issuance Date	4/26/2022	10/12/2022	10/25/2022	11/9/2022	12/7/2022
Size (\$MM)	214.0	424.1	284.2	153.0	315.8
Structure	100% Guaranteed	Senior/Sub	Senior/Sub	Senior/Sub	Senior/Sub
Senior Subordination (%)	0.0	20.0	15.0	25.0	25.0
Collateral Type	Preservation	Rehab Loan	Preservation	Rehab Loan	Rehab Loan
Sponsor	Merchants Bank of Indiana	ACRE Credit Partners REIT	Merchants Bank of Indiana	Harbor Group International	Arbor Realty SR
# of Loans	14	11	16	8	11
# of Properties	14	11	16	9	21
Typical Prepayment Provision	LO(11), 1%(69), O(4)	YM1%(15), O(21)	LO(12), 3%(11), 2%(12), 1%(48), O(1)	PP(18), O(18)	MI(17), O(19)

Source: Deal documents and Academy Securities

The different provisions may result in varying prepay trajectories across Q deals, even with limited rate-driven refi incentives for borrowers. Property change-of-ownership plays a key role in multifamily prepay activity, as we showed in a previous [report](#).² To be sure, multifamily transaction activity has significantly trended down. The quarterly national apartment sales volume dropped to \$50.7 billion late last year, compared to \$151.7 billion in January 2022, according to RCA (Figure 3). But with no lockout loans, or amid declining yield maintenance penalties in a higher rate environment, plenty of multifamily borrowers may still find it advantageous to prepay. Interestingly, “acquisition” is the dominant loan purpose across most 2022-vintage Q deal loans, except for the loans in Q-019 and Q-017, where “refinance” is much more prevalent.

Figure 3. US National Apartment Sales Volume, 2018-2022 (\$ Billions)



Source: Bloomberg, RCA, and Academy Securities

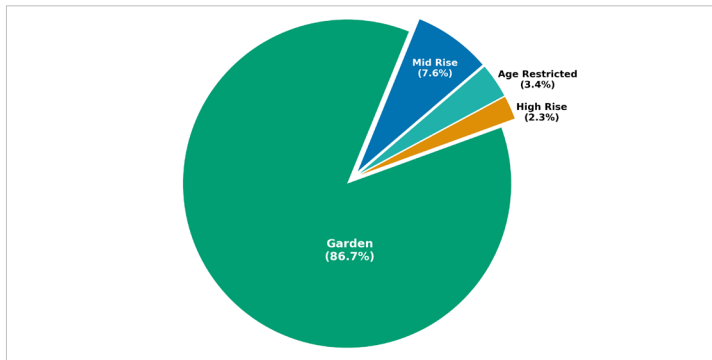
² “Multifamily Prepays: Property Sales Trigger Paydowns,” Securitized Products Special Topics, Academy Securities, August 10, 2022

Minimal Delinquencies, Preferred MF Subtype, and “Social” Exposure

We highlight a few other aspects to note as investors evaluate Q-deal exposures:

- Benign delinquencies underscore prepay focus.** Recent performance data make it clear that the key cashflow consideration for Q-deal bonds, even the unguaranteed ones, is indeed prepayments rather than delinquencies. 99.86% of Q loans are current according to Freddie’s latest performance report. Three loans are in special servicing (<1bp of outstanding balance). Total losses across all Q issuance also represent a minimal <1bp of total issuance. Interestingly, the largest delinquent loan in the October 2022 performance report (\$12.2 million, 424 South Broadway in Los Angeles, CA, also the second largest exposure in Q-010), is no longer reported as delinquent in the November 2022 performance report. A couple flags to track do pop up from the very benign Q collateral performance: (1) even a handful loan delinquencies can quickly ramp up the delinquency rate across individual deals given the small number of loans across most deals. Current delinquencies cluster in Q-010 (10.4%) and Q-007 (2.8%); (2) The loan watchlist rate is elevated across Q deals, at 20.1% of the outstanding loan population, according to Freddie. Property performance issues represent the major driver of watchlisting those loans.
- Mostly favorable subtype exposure, with some exceptions.** The recent Q deals feature exposure to multifamily subtypes that we consider well-positioned for evolving lifestyle preferences. This echoes our findings for other small balance multifamily deals, such as [FRESB](#).³ Nearly 87% of 2022-vintage Q-deal collateral is garden-style multifamily (Figure 4). Other multifamily subtypes sporadically appear across deals, with a few exposures to track. For example, The Residences at Merrillville Lakes, the largest exposure in Q-021 (\$46.8 million, 14.8% of the deal’s balance) is an age-restricted property in Merrillville, IN. In Q-019 the largest exposure, The Pomelo (\$62.5 million, 22%), is a 259-unit, newly constructed mid-rise building in Miami Gardens, FL. In turn, Q-017 has elevated exposure to mid-rise or high-rise properties in the Bronx, NY (across four loans, \$58.2 million, 27.2%). The unique dynamics of the New York multifamily market, such as rent regulations, may impact performance, as we discussed in a previous [report](#).⁴

Figure 4. 2022-vintage Q-Deal Property Subtype Distribution



Source: Freddie Mac and Academy Securities

³ “Small Balance Multifamily: Value in Concentrated Exposure Ahead of Slower Prepays,” Securitized Products Special Topics, Academy Securities, September 13, 2022

⁴ “NYC Multifamily: Rent Increases to Support Cashflows Amid Regulatory Restrictions,” Securitized Products Special Topics, Academy Securities, July 7, 2022

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- **Social bonds.** Three outstanding Q deals (Q-019, Q-017, and Q-014) are designated as “social bonds”, according to Freddie’s most recent Impact Deal performance report. Social bonds go beyond affordability by financing housing for “targeted populations” or providing liquidity to “social impact institutions”. The Q deals that meet Freddie’s social bond criteria may potentially see a wider investment base. The guaranteed bonds across such deals may qualify for Community Reinvestment Act (CRA) credit, the GSE states.

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