



Benchmarking Cap Rates and Prepayment Penalties in the Multifamily Sector

Key Takeaways:

- A total of 2,398 Freddie Mac, Fannie Mae, CMBS, and CRE CLOs multifamily loans in Trepp’s dataset were paid off prior to their maturity date.
- In 2021, 47 states had at least one loan that paid off prior to its maturity. The average prepayment penalty percent across the dataset was 5.24%.
- The states with the largest number of prepayments were Texas, California, and Georgia.

Since the beginning of the pandemic, the multifamily sector has served as a bright spot in what was otherwise a dark patch for commercial real estate. Economic shutdowns and stay-at-home orders initially kept occupancy and rents stable, and in the past year, multifamily sales have continued to see an uptick. An unseen byproduct of the resilience of the CRE sector was prepayments.

In 2021, a total of 2,398 multifamily loans were paid off prior to their maturity date. These loans are worth noting due to the nature of early payoffs in the securitized loan universe. In almost every instance when a securitized loan pays off prior to its maturity, the borrower must pay a prepayment penalty (either in the form of yield maintenance or a stated premium represented as a percentage of the loan balance). The reason prepayment penalties exist is simple; they allow the bondholder(s) to remain “whole” and achieve the same yield as if the borrower made all scheduled mortgage payments until loan maturity. In 2021, the majority of pre-maturity dispositions were loans that were originated with yield maintenance versus with a premium.

Why This Matters

For the sake of added context, let’s use an example; If a borrower has a \$10 million loan and is willing to pay a \$1 million yield maintenance charge. The implied value of the property is at least \$11 million, and likely considerably higher than that. If a borrower is willing to pay off a loan with yield maintenance it likely reveals one of two things: Either a)

someone has agreed to buy the property from the owner for more (and perhaps considerably more in this market) than the property was valued at securitization, or b) the owner of the asset can refinance the asset with new loan proceeds on a value that is considerably higher than the value of the collateral at the loans origination. Prepayments with yield maintenance or fixed penalties help encapsulate that property values have risen and are a positive sign for commercial real estate as a whole.

FIGURE 1: PREPAYMENT BY DISTRIBUTION TYPE

DISPOSITION TYPE	LOAN COUNT	AVG PENALTY %	AVG CAP RATE
Prepay w/ Yield Maintenance	1362	6.94	7.90
Prepay w/ Premium	1036	2.14	6.36

Source: Trepp

Analyzing the 2,000+ Loans

Of the 2,398 Freddie Mac, Fannie Mae, CMBS, and CLO multifamily loans in Trepp’s dataset that were paid off prior to their maturity date, 1,362 loans were prepaid with yield maintenance while 1,036 prepaid at a premium. The average prepayment penalty, however, had a large divergence. The loans with yield maintenance averaged a penalty of 6.94% versus a 2.14% prepayment penalty for loans that paid off with a premium. This is most likely due to the loans with a premium being slightly more seasoned loans where the prepayment exposure was less for the borrowers involved.

Additionally, Trepp reviewed the capitalization rates of the loans prior to their pre-maturity payoff. The data showed the average cap rate for loans with yield maintenance was 7.90% versus 6.36% for loans that prepaid with a premium.

To parse the data further, the loans were stratified by loan balance and seasoning. Approximately 55% of the loans that were prepaid had a balance of less than \$5 million at the time of prepayment. Considering the state of the multifamily market over the past year (with rapid increases in rental rates, compression of capitalization rates, and increased property values), it is understandable that loans of this size are being prepaid prematurely. The borrowers on these properties could absorb the increased prepayment expense due to the significant increases in the property's value.

FIGURE 2: PREPAYMENTS BY LOAN SIZE

LOAN SIZE BUCKET (AT DISPOSITION)	LOAN COUNT	AVG. PENALTY%	AVG. CAP RATE
< \$5 Million	1309	5.07	7.40
\$5-10 Million	391	6.00	7.80
\$10-20 Million	323	4.59	7.02
\$20 Million +	375	3.21	6.23

Source: Trepp

FIGURE 3: LOANS BY LIFECYCLE

LOAN SEASONING	LOAN COUNT	AVG. PENALTY%	AVG. CAP RATE
0-12 Months	14	5.54	2.99
12-24 Months	177	3.39	5.48
24 - 36 Months	322	4.09	6.02
36 - 48 Months	313	5.75	6.23
48 - 60 Months	407	5.72	6.94
60-72 Months	297	5.26	7.12
72 - 84 Months	224	5.90	7.68
84 - 96 Months	142	7.69	9.03
96 Months +	502	3.13	8.95

Source: Trepp

An analysis of the lifecycles of the loans shows that last year's multifamily prepayments largely came for loans with 96 months or more of seasoning. The second-largest category was those loans securitized 46-60 months ago. The average prepayment penalty was between 5-6% for five of the time-based categories, while loans seasoned between

84-96 months paid off with an average prepayment penalty of 7.69% and had an average cap rate of 9.03%.

Geographic Trends

Lastly, the Trepp team broke down the data geographically and by rate type. In 2021, 47 states had at least one loan that paid off prior to its maturity. The average prepayment penalty percent across the dataset was 5.24%, and the average cap rate was 4.34%.

The states with the largest number of prepayments were Texas, with 436 loans, followed by California, with 264 loans, and Georgia, with 170 loans. These states averaged prepayment penalties of 5.61%, 3.52%, and 4.88%, respectively.

The metro area with the largest number of loans that paid off with a penalty was the Dallas-Fort Worth-Arlington, TXMSA, with 182 loans. The average penalty was 6.31%, and the average cap rate was 4.06%. Dallas toted one of the highest average penalties on top of its high number of prepaid loans, despite the MSA making up only 42% of the loans that prepaid in the state of Texas.

FIGURE 4: TOP 5 STATES BY PREPAYMENT COUNT

STATE	LOAN COUNT	AVG. PENALTY %	AVG. CAP RATE
TX	436	5.61	4.19
CA	264	3.52	4.13
GA	170	4.88	4.20
FL	164	4.42	4.04
NY	115	2.61	4.22

Source: Trepp

FIGURE 5: TOP 5 MSAS BY PREPAYMENT COUNT

MSA	LOAN COUNT	AVG. PENALTY %	AVG. CAP RATE
Dallas-Fort Worth-Arlington, TX	182	6.31	4.06
New York-Newark-Jersey City, NY-NJ-PA	150	2.72	4.10
Los Angeles-Long Beach-Anaheim, CA	125	2.96	4.04
Atlanta-Sandy Springs-Roswell, GA	123	4.51	4.16
Houston-The Woodlands-Sugar Land, TX	113	3.94	4.25

Source: Trepp

The state with the highest prepayment penalty at the time of disposition was Nebraska, however, it was across only four loans. For states with more than ten loans that prepaid, New Mexico (11 loans, 8.78% average penalty), Kentucky (16 loans, 8.71% average penalty), Kansas (13 loans, 7.97% average penalty) and Ohio (57 loans, 7.35% average penalty) all posted distinctively higher than average penalties.

For MSAs with more than ten loans that prepaid with a penalty, the highest average penalty was 13.46% in Augusta-Richmond County, GA-SC followed by Louisville/Jefferson County, KY-IN with a 9.64% average penalty.

Identify Acquisition Opportunities

For investors looking for off-market deals, these insights provide a new avenue for identifying a significant number of under-the-radar acquisition targets. This prepayment data can be pared down to zip code or submarket level and can lead to more acquisition opportunities. ***Schedule a demo*** with Trepp to identify multifamily properties in your market that fit the prepayment profile mentioned in this article.



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