

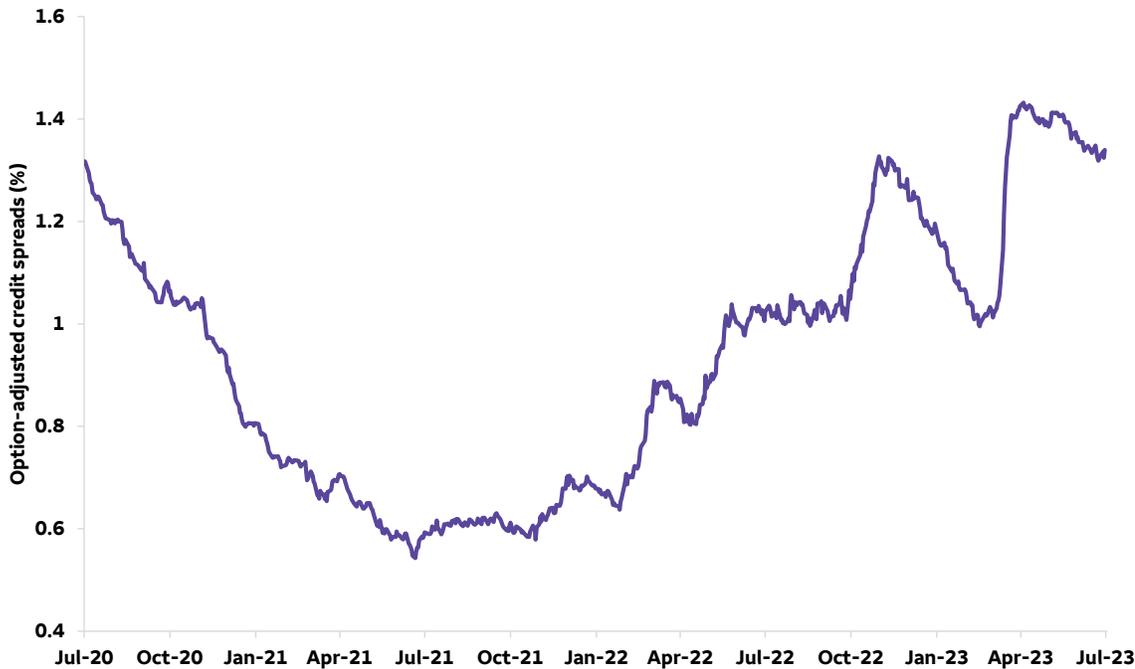


Chart of the Week

Weekly market analysis on key market indexes

July 17, 2023

Headwinds for commercial mortgage-backed securities



Sources: Wells Fargo Investment Institute and Bloomberg as of June 30, 2023. Commercial Mortgage-Backed Securities spreads are represented by the Bloomberg Commercial Mortgage-Backed Securities Index. An index is unmanaged and not available for direct investment. **Past performance is no guarantee of future results.**

Commercial mortgage-backed securities (CMBS) spreads remain elevated

Headwinds in commercial real estate (CRE) are widely known, and our belief is that conditions will likely continue to deteriorate. On June 13, 2023, we downgraded CMBS from neutral to unfavorable.

Not surprisingly, spreads on CMBS have widened notably over the past year. (Widening spreads can indicate that markets are concerned about the future.) We also see the market starting to differentiate among the various credits. While triple-A (AAA) and double-A (AA) spreads have declined slightly since May, the spreads on triple-B (BBB) remain elevated. Rating agencies have started to downgrade credit ratings and are applying renewed scrutiny to CMBS in reaction to concerns about cash flows, the demand for CRE space, and property valuations.

What it may mean for investors

For investors willing and able to bear the risk, we prefer higher-quality and short-to-intermediate duration (a measure of interest-rate sensitivity) in the AAA CMBS sectors. CMBS represent less than 2% of the Bloomberg U.S. Aggregate Bond Index; hence, investors should be aware that these investments can be illiquid.

Luis Alvarado, Global Investment Strategist

This chart was excerpted from the *Investment Strategy* report dated July 10, 2023

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Risk Considerations

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Commercial Mortgage-Backed Securities (CMBS)** are a type of mortgage-backed security backed by commercial mortgages rather than residential real estate. CMBS tend to be more complex and volatile than residential mortgage-backed securities due to the unique nature of the underlying property assets.

Definitions

Bloomberg Commercial Mortgage-Backed Securities Index measures the market of US Agency and US Non-Agency conduit and fusion CMBS.

Bloomberg U.S. Aggregate Bond Index is a broad-based measure of the investment grade, US dollar-denominated, fixed-rate taxable bond market.

An index is unmanaged and not available for direct investment.

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