



Use of Rating Trends in CMBS

CMBS is the only Structured Finance asset class that regularly uses trends, due to its ongoing surveillance approach. Similar to the Corporate sector, each DBRS rating category is appended with one of three rating trends - “Positive”, “Stable”, or “Negative”. The rating trend helps to provide an understanding of DBRS’s opinion regarding the outlook for the rating; although a positive or negative trend does not necessarily indicate that a rating change is imminent.

CMBS has an inherent positive trend when there is amortization and asset appreciation; however no pool is static. Property net cash flows increase or decrease at different rates and as a result of this, and other market factors, assets generally appreciate at different rates; although not all assets will appreciate. Rating trends allow DBRS to identify a general credit shift in the absence of critical information and to remain proactive when positive or negative factors impacting the asset pool are insufficient to warrant a change in the rating, but it can be determined that the pool has improved or worsened. Negative events may be offset by positive events, resulting in stable trends.

POSITIVE TREND

Ratings reflect the risk of the first dollar loss (or default) for the rated class; therefore DBRS generally uses a Positive trend when the majority or part of a class is considered to be in the rating category immediately above the rating category for the class, but the entire class is not in that rating category. DBRS upgrades the rated class once the entire class warrants the rating.

Examples of when DBRS uses Positive trends include when substantial pay-down from amortization or repayment of loans occurs and when a loan defeases with Government of Canada securities. These events are recognized as positive credit changes, though the changes are not large enough to support the upgrade of the entire class.

NEGATIVE TREND

A Negative trend indicates that negative events may have occurred or that unfavourable changes in respect of the asset pool are likely to occur in the near future, such as an adverse selection, a significant percentage of the pool being noted as loans that have a higher propensity for default, or the acquisition of new specially serviced loans without loss estimates.

STABLE TREND

A Stable trend indicates DBRS’s view that the rating is secure and that according to on-going surveillance and performance updates, the trend is stable.



TREND VS. IMPLICATION NOTATIONS

When a rating is placed “Under Review”, DBRS indicates its status as “Under Review with Positive, Negative, or Developing Implications”, as the case may be. The difference between a Positive trend and an Under Review with Positive Implications, for example, is primarily the timing of any related rating change. An Under Review with Positive Implications is generally used when a rating upgrade is imminent. However, as discussed above, a Positive trend may identify positive credit changes within the asset pool, but be insufficient to warrant a rating upgrade.

For further information regarding rating trends generally, please refer to DBRS policy “Rating Trends”, and regarding Under Review rating status, please refer to the DBRS policy “Under Review”.