

# An Empirical Study of the Determinants of Security Design in the CMBS Market

Christopher Downing and Nancy E. Wallace\*

June 3, 2005

## Abstract

In an efficient capital market, Commercial Mortgage Backed Securities (CMBS) would have no economic value over and above the value of mortgage pools, since they simply repackage existing securities. Yet the growing importance of CMBS suggests that this security design has led to significant cost efficiencies relative to traditional lenders. Asset securitization, such as CMBS, appears in the theoretical literature as a mechanism to address three types of market imperfections: transactions costs; market incompleteness; and asymmetric information. Our empirical analysis suggests that the relationships between the security design of recent CMBS deals and the subordination structure and pricing of CMBS bonds are quite consistent with an asymmetric information explanation for pooling and tranching.

---

\*Please address correspondence to (Downing): Jesse H. Jones School of Management, Rice University, Houston, TX 77005. (Wallace): Haas School of Business, University of California at Berkeley, Berkeley, CA 94720.