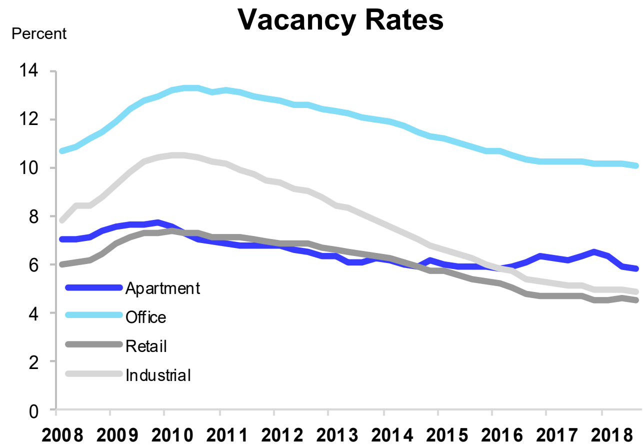
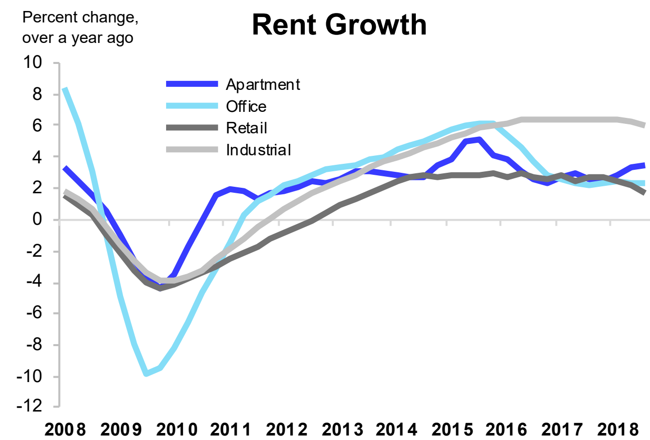
Nareit® Commercial Property Update 2018: Q3

Commercial real estate markets firmed in the third quarter





Apartment

Apartment markets continued to tighten in the third quarter of 2018, easing worries of over supply. Demand continued to outpace completions, causing vacancy rates to decrease for the third consecutive quarter, to 5.8 percent. Rent growth accelerated in the third quarter to 3.2 percent over the prior four quarters, compared to 2.6 percent growth a year ago. The return of higher rent increases suggests that there is substantial demand for apartment housing, even as the homeownership rate rises.

Retail

Retail markets enjoyed an uptick in demand, despite headline store closures. New supply slowed, resulting in excess demand for retail space, and vacancy rates fell five basis points to 4.5 percent. Rent growth continued to decelerate, despite greater interest in retail space, growing 1.6 percent over the prior year. Sears is the latest casualty for store bankruptcies. Landlords, however, remain optimistic about the long-term outlook as they'll be able to redevelop the space and reset rents paid.

Office

Office markets firmed in Q3 with demand trending up in comparison to prior quarters. Supply also lagged, helping vacancy rates edge downward to 10.0 percent, the low for this expansion. While demand rebounded compared to previous months, it remains below this cycle's peak in 2015 and significantly below peak demand of the prior cycle. Rent growth remained steady at 2.2 percent growth over the prior year.

Industrial

Industrial property markets show no sign of slowing. Net new leases absorbed 58.8 million square feet of new space, matching the amount of new supply. Vacancy rates held steady, standing at 4.8 percent. Rent growth decelerated slightly, but remains elevated at almost six percent over the past four quarters. Growth in e-commerce continues to bode well for the long-term outlook of the industrial sector.

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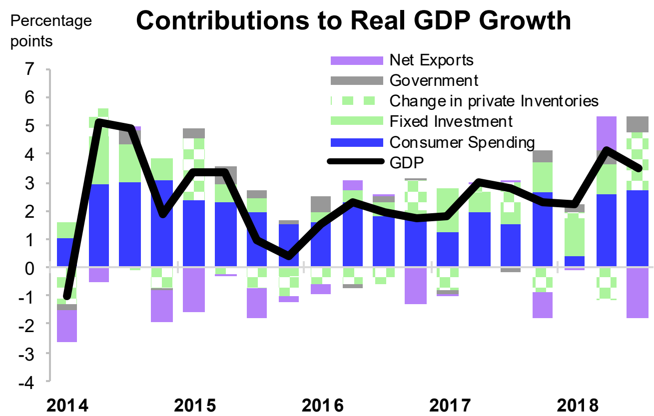
Source: Data from CoStar and Nareit 2018.

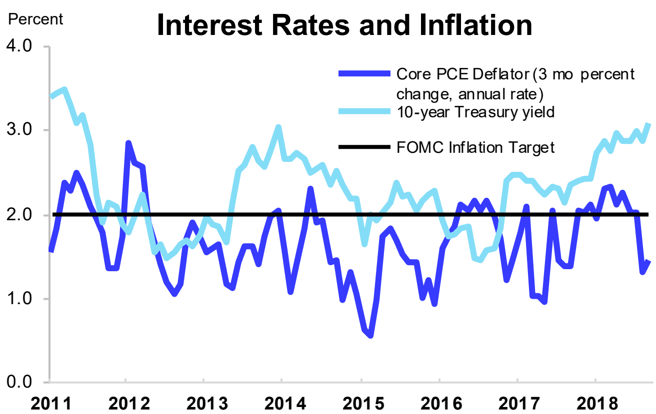
Economic activity boosts CRE fundamentals



Economic momentum continues in Q3

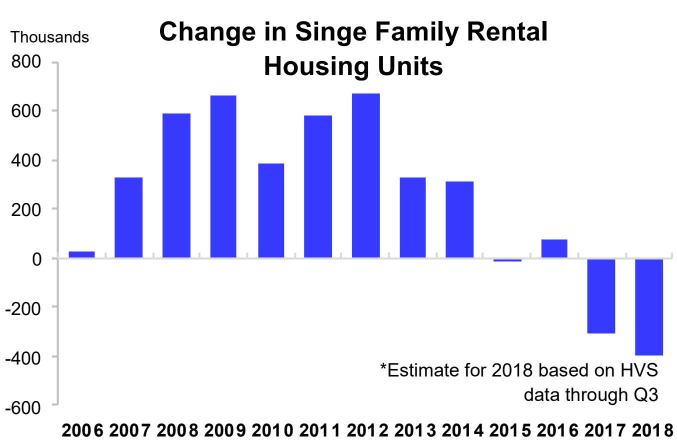
Economic growth slowed just a bit in the third quarter, to a 3.5 percent annual rate. Consumer spending remained robust, rising 2.7 percent (blue bars show the contribution to total GDP growth, the solid line). Fiscal stimulus from last year's tax cuts have boosted growth in 2018, although this effect is expected to fade next year.

The job market remains vigorous, with employment rising 250,000 in October. Average hourly earnings accelerated as well, to a 3.1 percent increase over the past 12 months, the highest since 2009.



Inflation moves below Fed's target

Inflation slowed to a 1.5 percent annual rate in the three months through September, moving back below the Federal Reserve target of 2 percent. A jump in inflation earlier in the year had fanned fears that the Fed was "behind the curve" in removing the monetary stimulus it had put in place during the Great Recession, but recent trends suggest a more moderate inflation and interest rate outlook.



Home ownership and rental homes

The number of single family rental homes fell by 400 thousand units in 2017, marking a turning point in homeownership. Home rentals rose sharply during the housing crisis, reflecting severe household financial distress. Recent declines suggest that household financial positions are buoyed by rising jobs and incomes. This is favorable news for GDP growth as a stronger household sector tends to drive the overall economy. The trend in rental homes is responsible for the rising homeownership rate. Demand for apartment rentals also remains solid, but the sale of rental homes to new homeowners has offset increases in apartment rentals.

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Source: Data from BEA, BLS, U.S. Census Bureau and Nareit 2018.