



Capital Markets

Real estate office investors practiced patience in 2022, after a hectic 2021 that saw sales volume spike as investors looked to diversify assets and take advantage of owners looking to reduce risk. However, office sales volume fell every quarter in 2022 as interest rates increased and market valuations in the office sector dropped.

Meanwhile, industrial owners looked to capitalize on a red-hot market and pocket gains as demand pushed up lease rates. In many instances cap rates for industrial properties fell below current borrowing costs.

Occupier View

Trends

- Office occupiers prepare for the possibility their building is in distress
- Industrial owner/users consider sale-leaseback options

Look Ahead

- Occupiers seek assurances TIs and other amenities will be funded by landlords
- Depending on asset type, occupiers may have leverage on lease rates as new supply slows

Commercial Real Estate Capital Markets are at a Crossroads.

Factors Impacting Capital Markets

The volatility of 2022 led global central banks to raise interest rates to combat soaring inflation, ending a decades-long era of low inflation and historically low-interest rates. The dramatic increases in short-term interest rates led to many lenders staying on the sidelines and adjusting the pricing of risk assets, like real estate.

Setting the Stage

With the notable exception of older Class A and Class B and C office assets, real estate fundamentals are relatively strong. Future supply will be limited as construction costs rise.

Interest Rates

The Fed's hawkish approach to interest rates will likely be softened by the recent struggles of Silicone Valley Bank and others, but the rate has still been raised 9 times since March 2022.

Inflation

Inflation rates increased 0.4% in February, still higher than historic monthly increases, but has been growing at a slower rate compared to the increases from the first half of 2022.

Cap Rates Expand

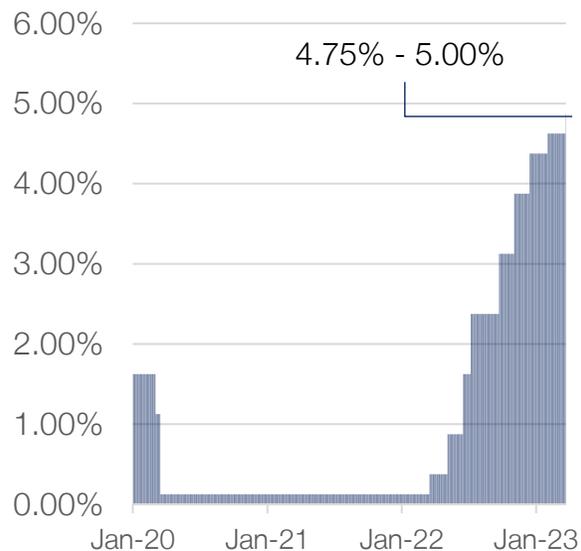
Capitalization rates have expanded in the near-term, impacted by economic volatility and monetary policy. The result of the higher cap rates has lowered pricing on acquisitions.

Capital Availability

Capital has been building for institutions looking to invest in CRE, but it is being deployed slowly as companies wait to see where market valuations are headed.

Federal Funds Effective Rate

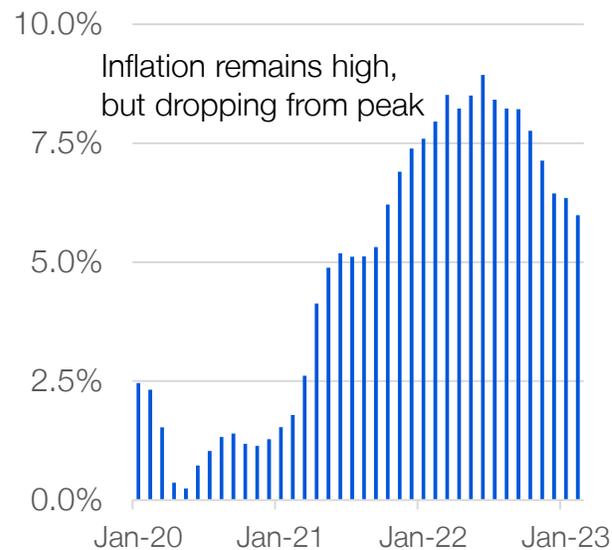
(As of March 2023)



Source: Board of Governors of the Federal Reserve System

Consumer Price Index

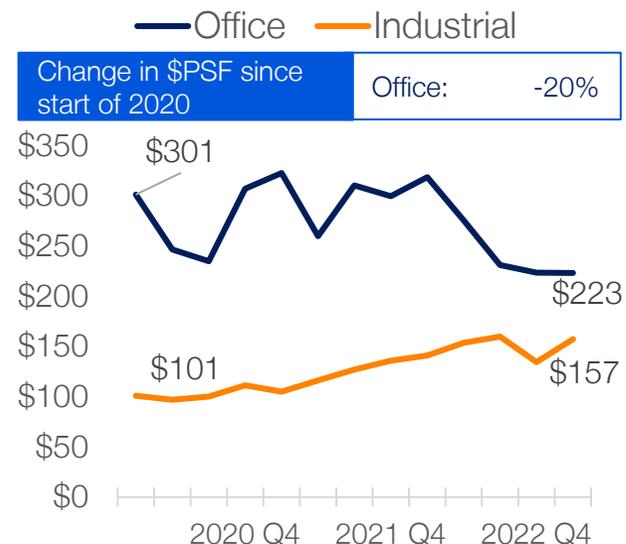
12-month change (All Categories)



Source: U.S. Bureau of Labor Statistics

Price \$PSF Change

(by Asset Type – US only)



Source: CoStar and Cresa



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