

Commercial Real Estate Trends & Outlook

April 2021

National Association of REALTORS®
Research Group



NATIONAL
ASSOCIATION OF
REALTORS®

COMMERCIAL REAL ESTATE TRENDS & OUTLOOK

April 2021 Report

The commercial real estate market is recovering but remains weak compared to conditions before the COVID-19 pandemic, according to NAR commercial members who responded to the 2021 Q1 Commercial Real Estate Quarterly Market Survey and industry data.

Acquisitions for large commercial real estate—properties or portfolios of at least \$2.5 million — fell 28% year-over-year in the first quarter of 2021, with transactions declining across all property types, except for hotel acquisitions. Investors could be acquiring hotels to convert into other uses such as multifamily housing.

Among commercial members of NAR who participated in the quarterly market survey and whose acquisitions were typically properties or portfolios of less than \$2.5 million, transactions declined by an average of 1%. Respondents reported an increase in sales of land and industrial properties and a decline in sales of other types of commercial real estate.

Commercial real estate prices continue to firm up, but the value of commercial real estate is still broadly down by 6% compared to one year ago.

A majority of NAR commercial members who responded to the 2021 Q1 commercial survey—70% — reported that companies are leasing or moving into office with small square footage due to working from home.

The commercial real estate market's recovery will remain uneven in 2021. Commercial members of NAR who responded to the survey anticipate a modest increase in sales of land (5%), industrial warehouses (3%), and Class B/C apartments (1%), but anticipate a decline in sales transactions of retail, office, and hotel/hospitality properties in the next 12 months.

However, commercial real estate transactions should experience a stronger recovery across all sectors in 2022 as more businesses operate at normal capacity, a larger fraction of the workforce returns to the office, and as business and leisure travel picks up strongly in 2022 with the broad swath of the population fully vaccinated, and assuming there is no resurgence of deadlier COVID-19 variants.

Enjoy reading the latest report!

1 | COMMERCIAL SALES

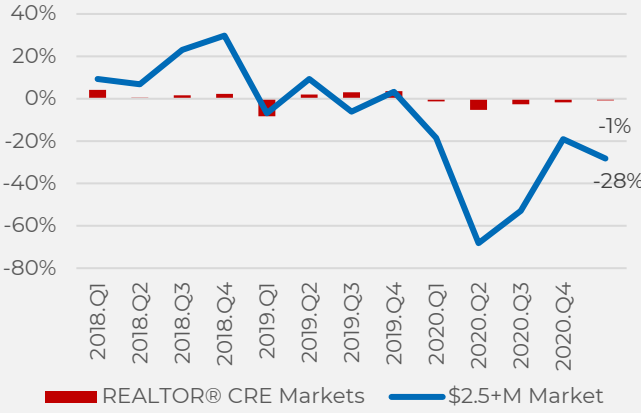
Commercial Sales Transactions Down 28% from One Year Ago

As businesses continue to operate below normal capacity and with people and businesses still holding back on travel and recreation with COVID-19 vaccinations still underway, commercial sales transactions continued to decline in the first quarter of 2021.

Commercial transactions of \$2.5 million and above decreased 28% from one year ago, according to Real Capital Analytics. Transactions were down across all property types except for hotel properties where acquisitions rose 13%. Investors could be acquiring some hotels to be converted into other uses, such as multifamily housing. Apartment buildings accounted for a third of the closed transactions.

In the small CRE market where transactions are less than \$2.5 million, NAR commercial members who participated in the 2021 Q1 Commercial Real Estate Quarterly Survey reported that their sales transactions volume in the first quarter of 2020 contracted on average by 1% compared to the level one year ago. Respondents reported an increase in acquisitions for industrial properties and all types of land, with strong growth in sales of residential and industrial land.

Quarterly Sales Volume (YoY % Change) as of 2021 Q1

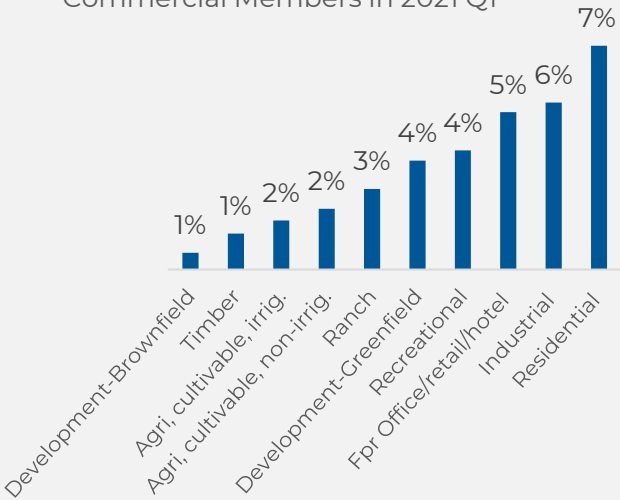


\$2.5 Million or More Transactions

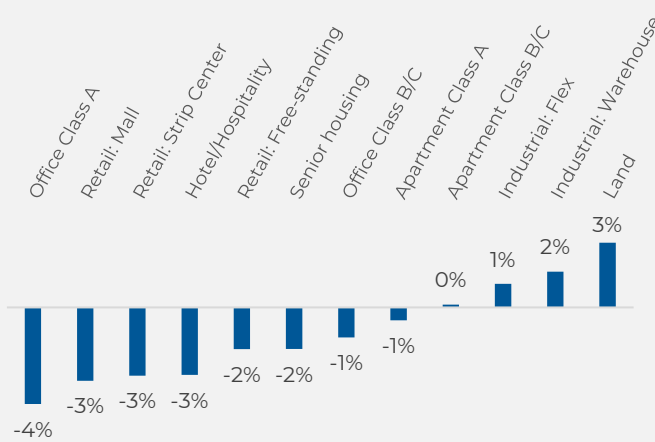
	Q1 '21	
	Vol (\$b)	YOY
Office	20.5	-36%
Retail	7.8	-42%
Industrial	19.6	-41%
Hotel	5.6	13%
Apartment	35.5	-12%
Seniors Housing & Care	3.3	-8%
Dev Site	4.3	-40%
Total	96.7	-28%

Real Capital Analytics

YoY % Chg of Land Sales Among NAR Commercial Members in 2021 Q1



YoY % Change in the Dollar Commercial Sales Volume in 2021 Q1 Among NAR Commercial Members



1 | COMMERCIAL SALES

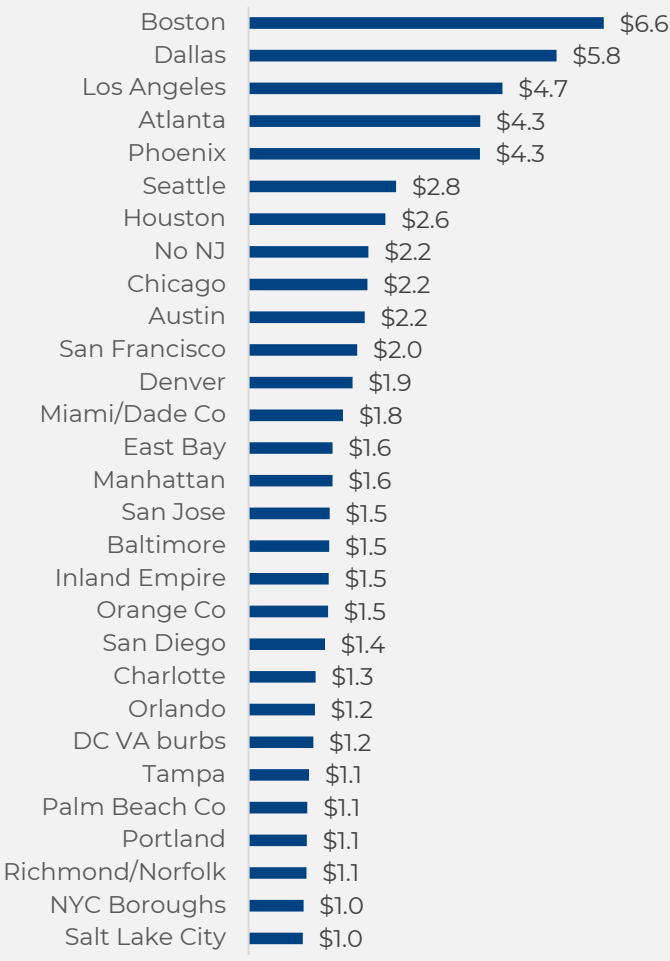
For deals of \$2.5 million or more, Boston, Dallas, Los Angeles, Atlanta, and Phoenix closed the most deal volume in the first quarter of 2021. Except for Boston, the top five markets are all non-gateway cities.

In Boston, the bulk of the deals were for office properties. In Dallas, Los Angeles, Atlanta, and Phoenix, a large component was for apartment properties.

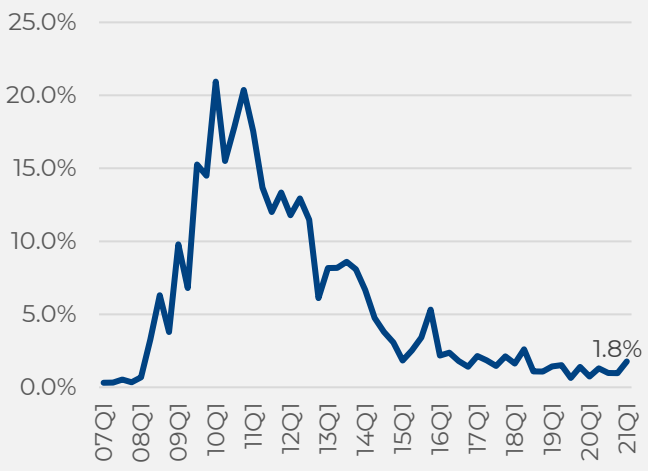
Distressed Sales at 2% of Total Transactions

Among transactions of \$2.5 million or over, distressed sales accounted for less than 2% of sales. Despite the rise in vacancy rates, there are little distressed sales compared to the Great Recession when distressed sales made up nearly 20% of sales. One reason is that investors like REITs are less leveraged this time compared to the Great Recession. During the Great Recession, the debt to total market capitalization (debt plus equity) of equity REITs market hit a peak of 57.5%.¹ As of March 2021, the debt to equity ratio is at 32.3%, according to Nareit.²

Commercial Transactions of \$2.5M or Over Closed in 2021 Q1 in Billion Dollars



Distressed Sales as a Percent of Total Sales of Properties \$2.5 Million or Over



Real Capital Analytics

Real Capital Analytics

1 Nareit, <https://www.reit.com/news/blog/nareit-media/equity-reits-have-lowest-debt-ratio-20-years>
 2 Nareit, https://www.reit.com/sites/default/files/2021-04/MediaFactSheet_Mar-2021.pdf

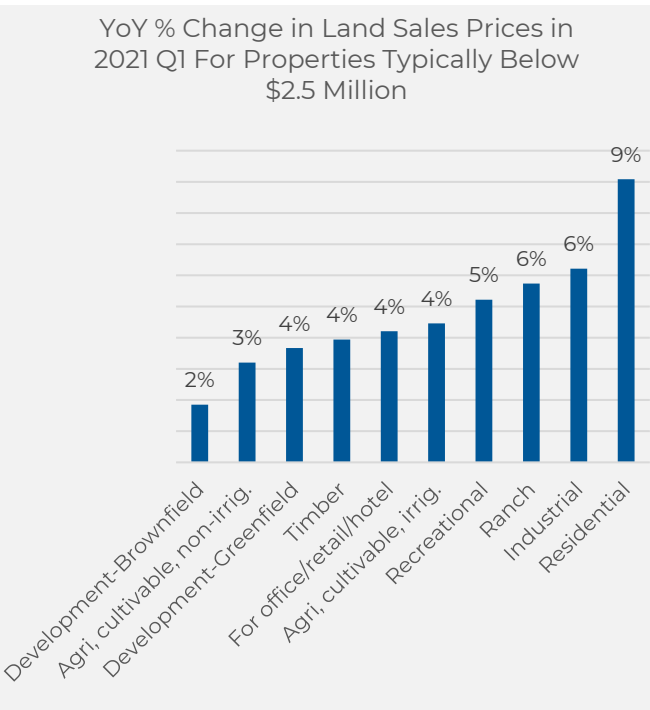
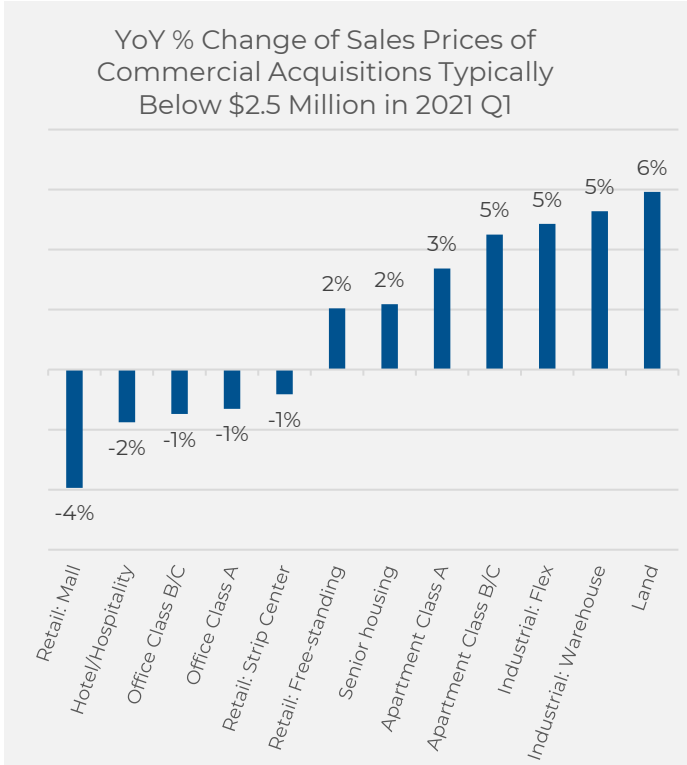
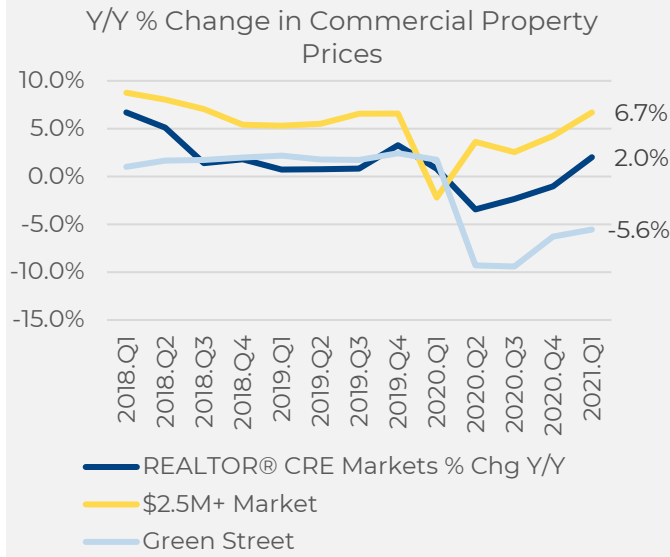
2 | COMMERCIAL PRICES

Commercial Prices are Recovering But Still Down 6%

Commercial real estate prices continue to firm up, but the value of commercial real estate is still broadly down by 6% compared to one year ago, based on the Green Street Commercial Price Index, an appraisal-based index of the properties held by REITs. The decline has tapered off from the 10% decline in the second quarter of 2020.

Among closed transactions valued at \$2.5 million or over, sales prices rose 6.7% from one year ago, according to Real Capital Analytics.

Among closed transactions of NAR commercial members which are typically below \$2.5 million, sales price rose by 2% on average. Respondents reported strong price gains for land (+6%), industrial warehouses (+5%), and class B/C apartments (+5%). Sales prices of residential land were up 9% on average, according to NAR commercial members.



2 | COMMERCIAL PRICES

Cap Rates on the Decline

As commercial prices continue to firm up, cap rates continued to decline. Apartment acquisitions had the lowest cap rate of 4.9%, followed by industrial at 5.9%. Hotel properties had the highest cap rates, at 8.6%. Office cap rates were at 6.6% .

Risk spreads (cap rate less 10-year T-note) for office, retail, industrial and hotel have also trended downwards and cap rates are now at about the same level in 2021 Q1 compared to one year ago. However, the market is still thin so these cap rates reflect transactions that are likely of prime properties or that are expected to yield good cash flows when redeveloped or put to other uses than the current revenue flows at the existing use.

The cap rates for properties typically below \$2.5 million tend to be higher than cap rates of properties that are typically valued at \$2.5 million or over. NAR commercial members reported the lowest cap rate for Class A apartment properties, at 5.7%, on average. Office acquisitions had a cap rate of 6.5% on average. Hotel and retail mail acquisitions had the highest cap rates, at over 8%, on average.

Cap Rates in 2021 Q1 Properties \$2.5 M or More

Office	6.6%
Industrial	5.9%
Retail	6.7%
Apartment	4.9%
Hotel	8.6%
Seniors Housing & Care	7.0%

Source: Real Capital Analytics

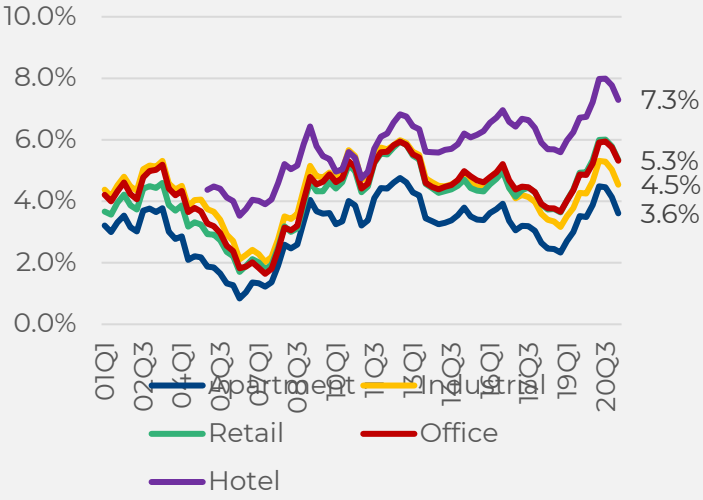
Cap Rates for in 2021 Q1 Properties Typically Less than \$2.5 M

Office: Class A	6.5
Office: Class B/C	7.2
Industrial: Warehouse	6.8
Industrial: Flex	6.8
Retail: Strip center	7.1
Retail: Mall	8.1
Retail: Free-standing	6.8
Apartment: Class A	5.7
Apartment: Class B/C	6.4
Hotel/Hospitality	8.2
Senior housing	7.5
Land	6.0

Source: 2021 Q1 NAR CRE Market Survey

For \$2.5 million or less properties

Risk Spreads for Properties \$2.5 Million or Over (Cap Rates Less 10-Year T-Bond)



Source: Real Capital Analytics

3 | LEASING

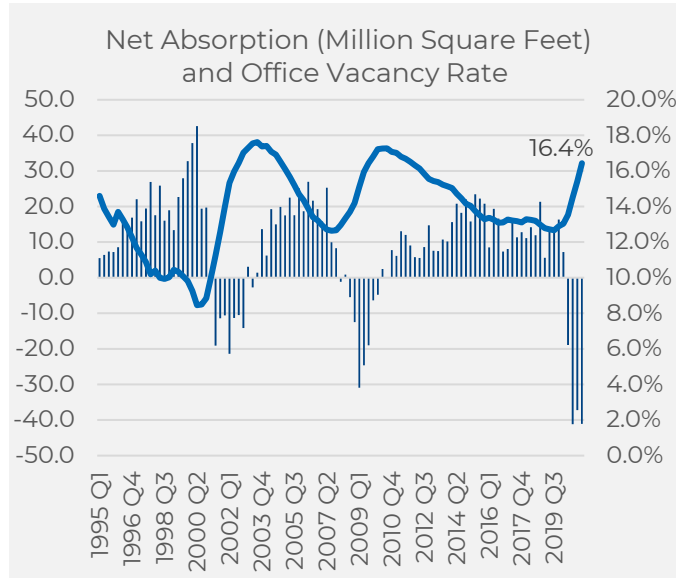
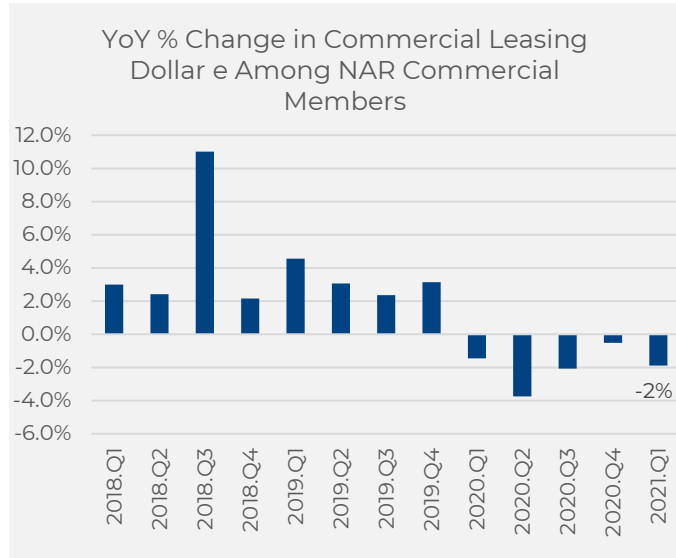
Leasing Activity for New Leases and Renewals Continues to Fall in 2021 Q1

For the fifth consecutive quarter, the dollar volume of new leases and renewals among properties leased or managed by NAR commercial members who responded to the survey fell by 2% on average in 2021 Q1.

Office Occupancy Continues to Fall While Industrial Occupancy Rises in 2021 Q1

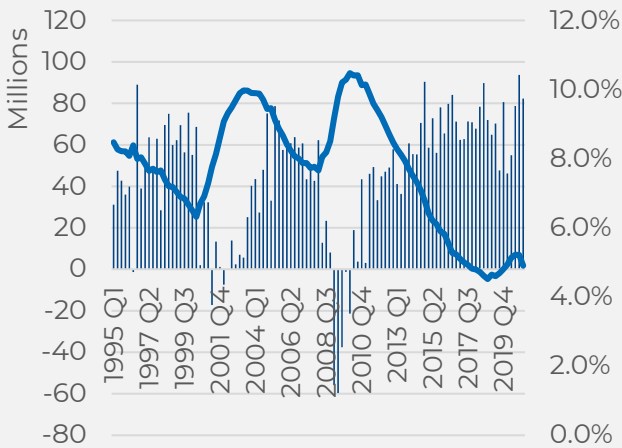
For the fourth consecutive quarter, office absorption was negative (-41.1 MSF), bringing the total negative net absorption since 2020 Q2 to 138.4 million square feet (MSF), according to Cushman and Wakefield market data. Office vacancy continued to rise to 16.4% from 13% in 2020 Q1.

On the other hand, occupancy in industrial spaces rose 82.7 million square feet in 2021 Q1 and totaled 309.7 million square feet during in the past four quarters. The increase in industrial absorption offsets the negative net absorption in the office sector (-138.4 million square feet (MSF)).



Sources: Cushman and Wakefield

Absorption of Industrial Space and Vacancy Rate



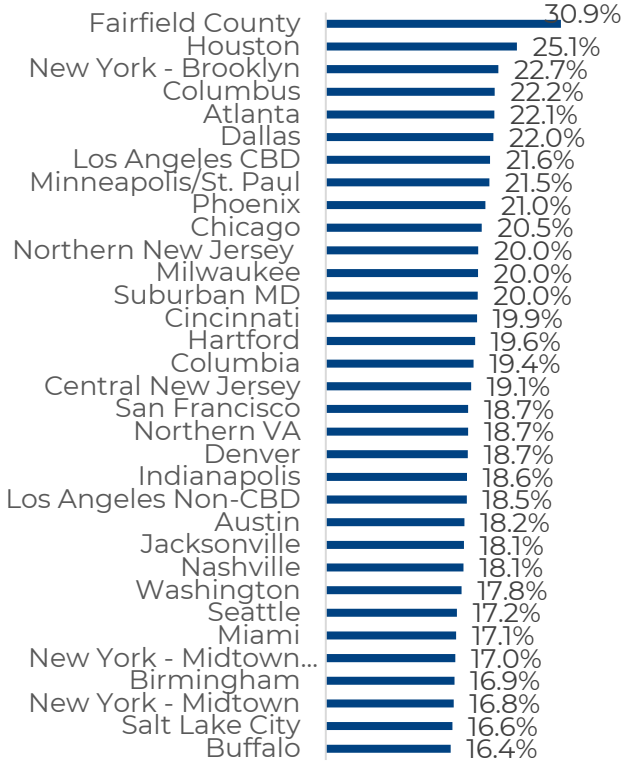
3 | LEASING

Office Occupancy Continues to Fall in 2021 Q1

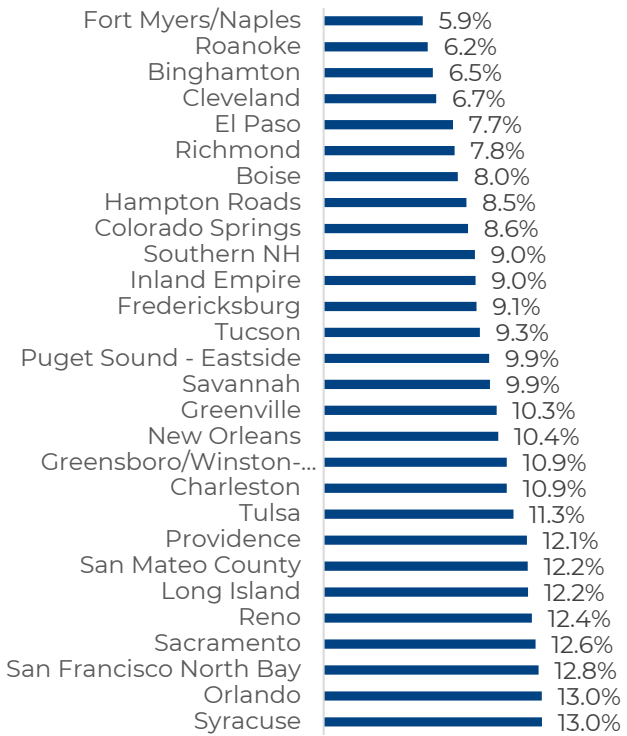
Major and/or gateway cities experienced vacancy rates above the national rate (16.4%) such as Fairfield County (Connecticut), New York, Chicago, Washington DC, Dallas, Houston, Los Angeles, San Francisco, and Seattle.

On the other hand, smaller or tertiary cities such as Fort Myers, Cleveland, El Paso, Richmond, Boise, Colorado Springs, Tucson, Puget Sound, Savannah, and Sacramento had office vacancy rates of less than 10 percent.

Vacancy Rates as of 2021 Q1



Vacancy Rates as of 2021 Q1



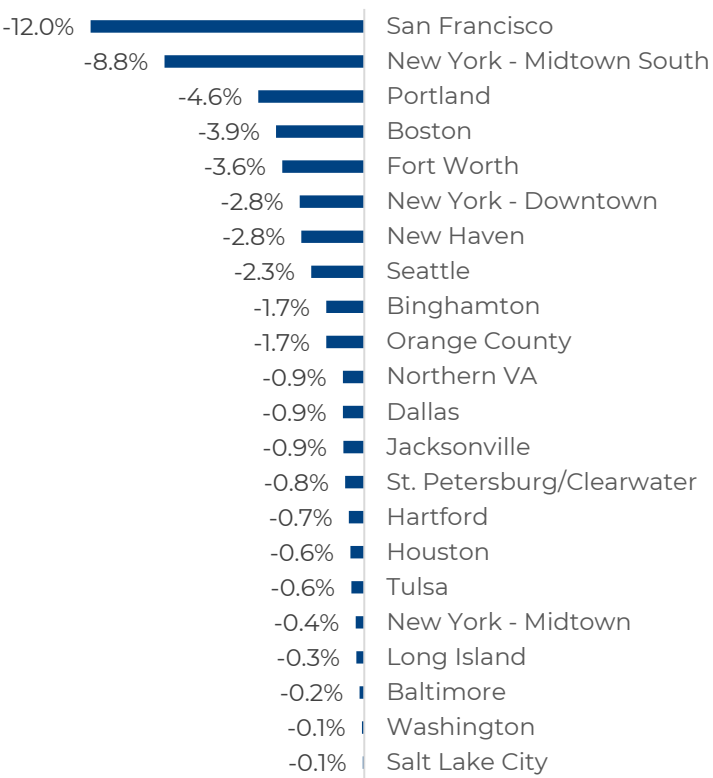
3 | LEASING

Office Asking Rents Up 5% But Landlords are Providing Concessions

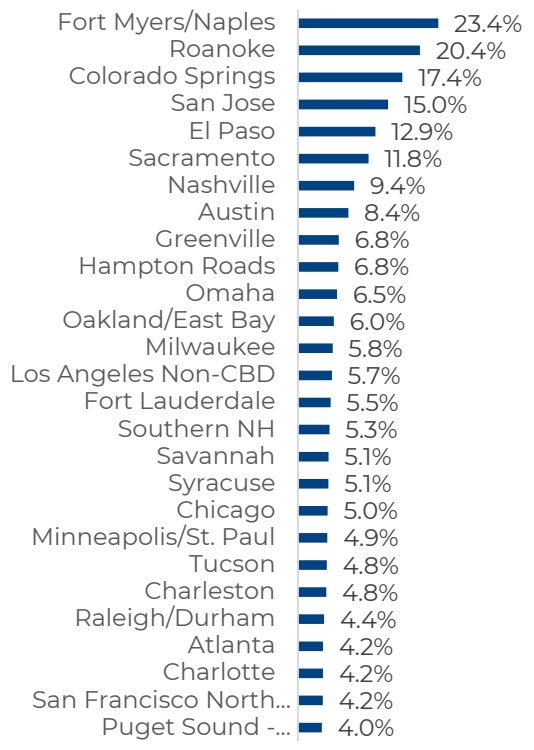
While office occupancy has fallen, asking rents were up 5% year-over-year. Asking rents have not declined but most landlords have been providing tenant concessions. Fifty-five percent of NAR commercial members who responded to the latest quarterly commercial survey reported that they are seeing more tenant concessions compared to the pre-pandemic period.

In the areas with high vacancy rates, asking rents have are still depressed, such as in San Francisco (-12%) and New York Midtown South (-9%). But in cities with low office vacancy rates, asking rents have sharply increased, such as In Fort Myers/Naples, Roanoke, Colorado Springs, El Paso, Sacramento, with asking rents at over 10%.

Year-over-year Percent Change in Office Asking Rent



Year-over-year Percent Change in Office Rent



Sources: Cushman and Wakefield

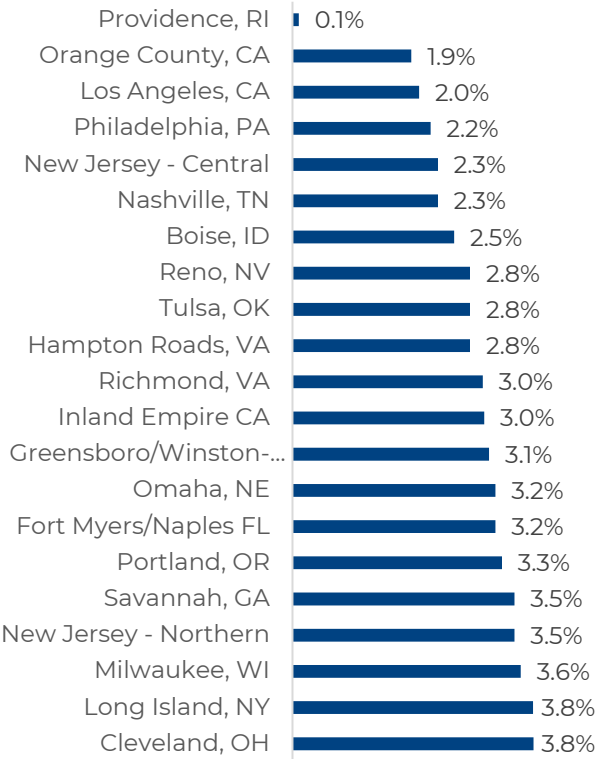
3 | LEASING

Industrial Occupancy Continues to Increase in 2021 Q1

During 2021 Q2 through 2021 Q1, Atlanta saw the largest increase in net absorption of industrial space, followed by the Inland Empire, Pennsylvania I-87/79 corridor, Chicago, and Dallas.

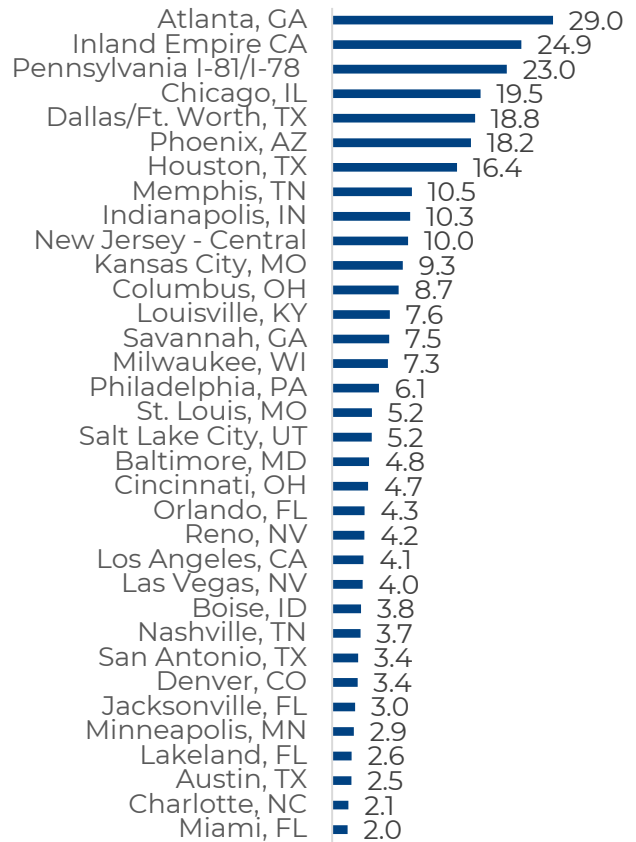
Industrial vacancy rate declined to 4.9 percent. The areas with the lowest vacancy rates include Providence, Orange County, Los Angeles, Philadelphia, and the New Jersey-Central area, Nashville, Boise, Reno, Tulsa, and Hampton Roads Virginia.

Industrial Vacancy Rate in 2021 Q1



Sources: Cushman and Wakefield

Industrial Net Absorption 2020 Q2-2021 Q1 in Million Square Feet



3 | LEASING

Trend Towards Smaller Square Footage, Shorter Term Leases, and More Suburban Leases

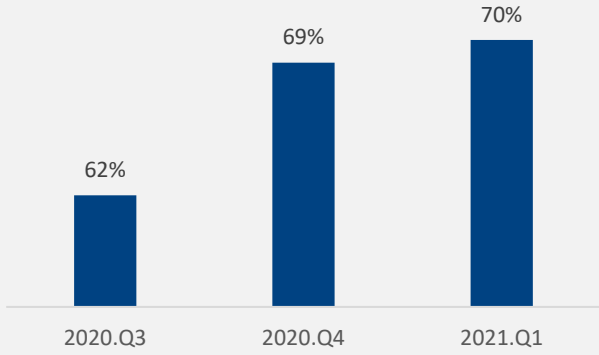
During the COVID-19 pandemic, working from home became the norm. A majority of NAR commercial members who responded to the 2021 Q1 commercial survey—70% — reported that companies are leasing or moving into office with small square footage due to working from home.

More than half of respondents— 57% — reported that they are seeing more short-term leases of less than 2 years compared to the case prior to the pandemic.

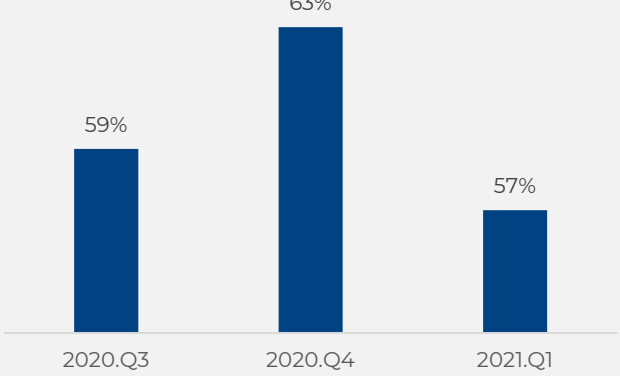
More than half of respondents — 55% — reported that more tenants are offering rent concessions, compared to the case prior to the pandemic.

While less than a majority of respondents reported — 47% — reported having more sales or leasing transactions in the suburban areas compared to the case prior to the pandemic, the rising share of respondents indicates an increasing preference of investors for properties in the suburbs than in the central business districts.

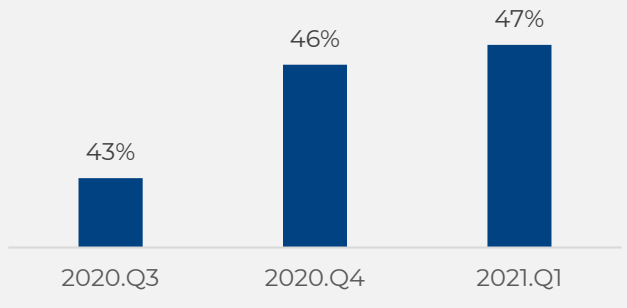
Companies leasing or moving into offices with smaller square footage due to working from home



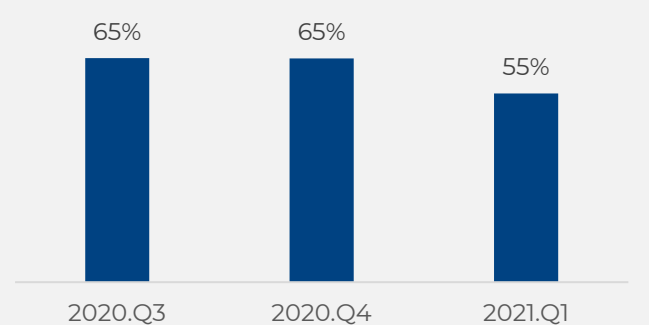
Percent of REALTOR® respondents who reported "More" short-term office leases of 2 years or less



Percent of respondents who reported "More" sales or leasing transactions in suburban area vs. central business district compared to January 2020



Percent of respondents who reported "More" landlords offering tenant rent concessions compared to January 2020



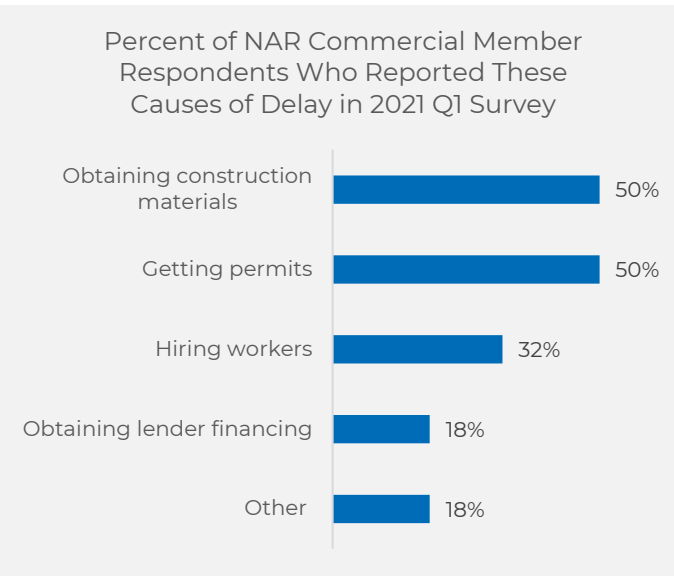
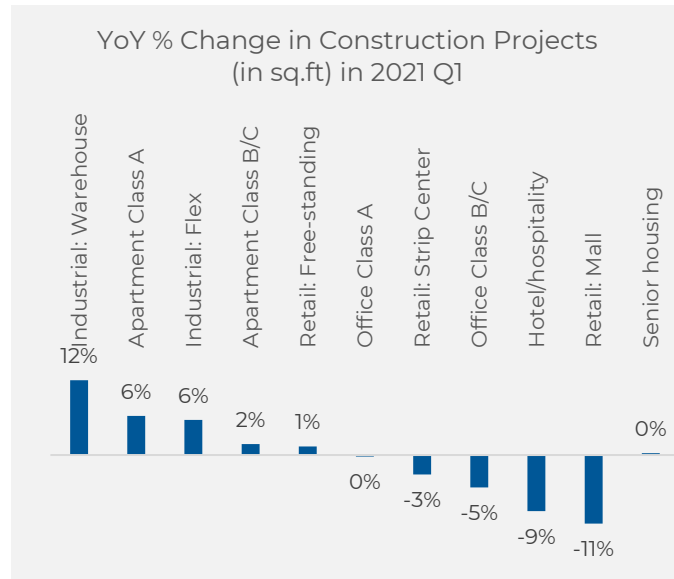
4 | CONSTRUCTION

More Residential and Industrial Development

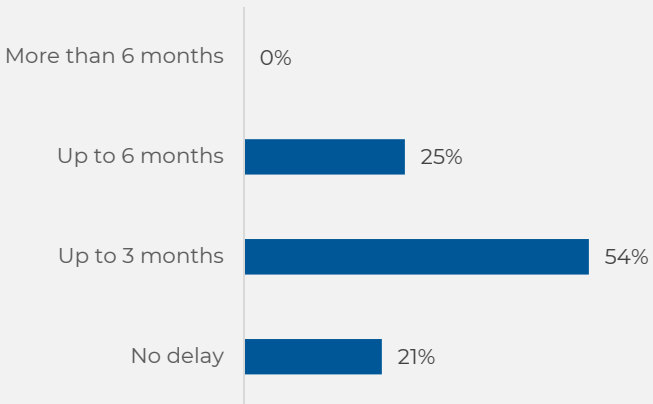
Commercial members of NAR who are engaged in construction/development reported that on average, their construction activity (in square feet) was up 1% from one year ago. On average, respondents reported a 12% year-over-year increase in construction activity (in square footage) for industrial warehouses. Construction activity was also up by 6% for Class A apartments and 2% higher for Class B/C. However, construction activity for retail malls, office, hotel, retail, and senior housing declined.

Respondents of the 2021 Q1 survey reported that obtaining construction materials and getting permits were the main factors causing construction delays, with half of respondents citing these causes. Hiring workers was cited by a third of respondents. Obtaining was cited by only less than 1 in 5 respondents, which indicates that obtaining financing is not a major issue for developers.

Delays were typically up to 3 months. No respondents to the 2021 Q1 survey reported a delay of more than 6 months.



Construction Delays Reported by NAR Commercial Members Engaged in Development in 2021 Q1 Survey



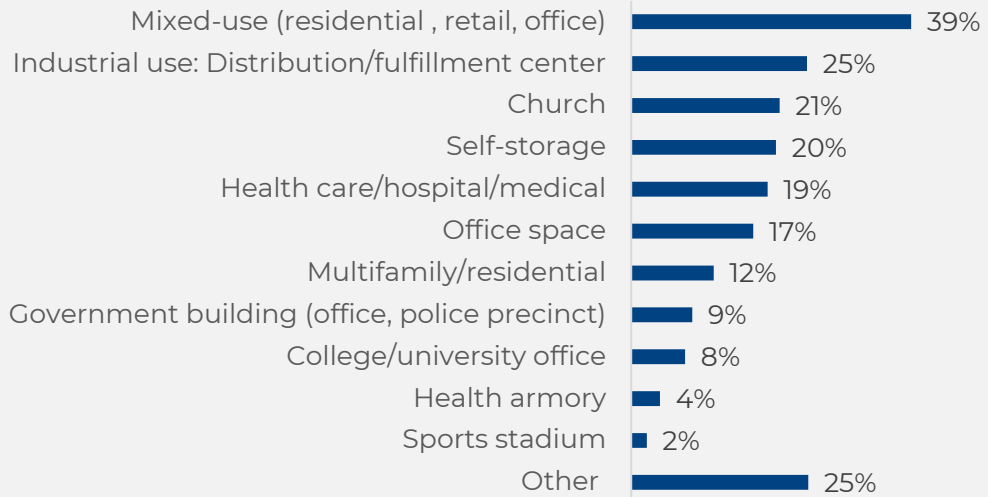
4 | CONSTRUCTION

Repurposing Vacant Malls

Vacant malls are being converted into other uses. In the 2021 Q1 survey, 39% of the reported responses were conversion of the vacant mall into a mixed –use project. The next most prevalent reuse was as a distribution center, a church, or a self-storage facility.

In 2020, NAR compiled a list of case studies on the conversion of vacant malls to other uses to provide a blueprint on how to finance the conversion and how state and local governments can support the conversion of vacant malls to other uses. Download the report [here](#).

How are vacant malls being repurposed in your market?
2021 Q1 Survey



5 | COMMERCIAL OUTLOOK

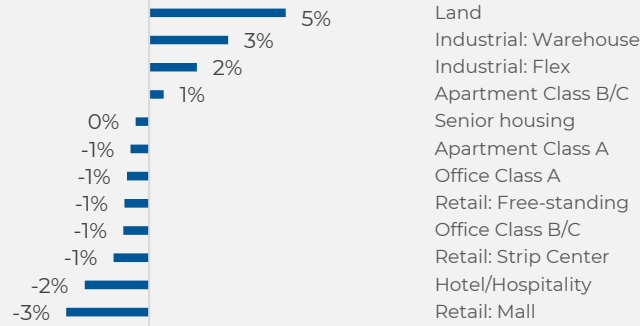
NAR Commercial Members Expect More Sales Transactions in Land, Residential, and Industrial Properties

Commercial members of NAR who responded to the survey anticipate a modest increase in sales of land (5%), industrial warehouses (3%), and Class B/C apartments (1%) in the next 12 months. Respondents anticipate a decline in sales transactions for retail, office, and hotel/hospitality properties.

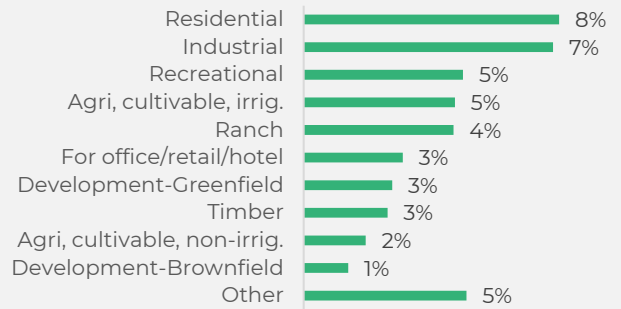
Pertaining to land sales, respondents anticipate strong sales growth for residential land (8%), industrial land (7%), and recreational land (5%), as well as agricultural land (5%).

Respondents expect commercial prices to increase in the next 12 months across most property types, except for office, retail, and hotel properties.

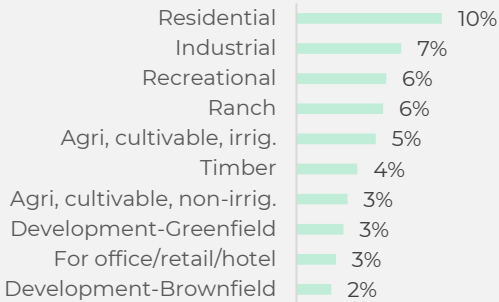
Expected Change in Dollar Sales Volume in the Next 12 Months Among NAR Commercial Members



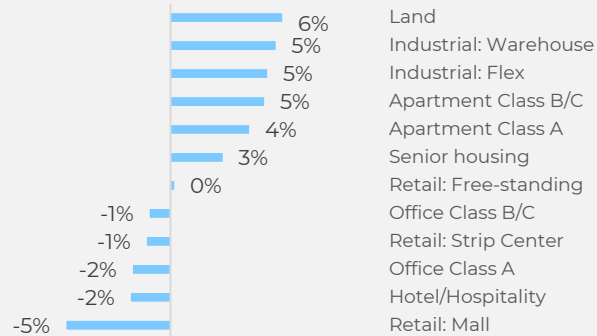
Expected Change in Dollar Land Sales in the Next 12 Months Among NAR Commercial Members



Expected Change in Land Prices in the Next 12 Months Among NAR Commercial Members



Expected Change in Commercial Prices in the Next 12 Months Among NAR Commercial Members



COMMERCIAL REAL ESTATE TRENDS & OUTLOOK

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This report is based on information collected from NAR's 2021 Q1 Commercial Real Estate Quarterly Market Survey. The survey asks about the commercial transactions of REALTORS® and members of NAR' commercial affiliate organizations (CCIM, SIOR, RLI, IREM, and the Counselors of Real Estate) during the fourth quarter of 2020. The survey was sent to approximately 76,000 commercial REALTORS® and members of affiliate organizations during April 1–22, 2021, of which 1,043 provided answers to at least one question. There were 346 respondents who reported a sales transaction, 153 respondents who reported a land sales transaction, 35 respondents who reported a leasing transaction, and 19 respondents who provided information on development transactions. Given the small sample size, the figures cited in this report should be treated with caution and should be interpreted as indicators of market trends rather than as accurate market statistics.

The NAR Research Group acknowledges the I/S/Cs for reaching out to their members to respond to the survey and developing the survey: Aubrie Kobernus, CEO, Realtors® Land Institute; Denise LeDuc-Froemming, CEO/EVP, IREM; Alexis Fermanis, Communications Director, SIOR; and Greg Fine, CEO/EVP, CCIM Institute. The Research Group also acknowledges Charlie Dawson, Vice-President, Engagement, and Rodney Gansho, Director of Engagement, in reaching out to CCIM, CRE, IREM, SIOR, and RLI designees to respond to the survey.

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