Current Trends in Commercial Real Estate - Is it Reaching a Peak?

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Consultant, NCREIF
Visiting Professor, Johns Hopkins Univ.
Annualized Returns for past 10 years

Leveraged Private Real Estate Outperformed REITs and Stocks

Private Institutional Commercial Real Estate

Publicly Traded REITs

Stocks
NCREIF Property Index (Unleveraged)

Returns from 1979 through 2015

Strong Double Digit Returns the Past 5 years since Recovery

Real Estate Returns
4 quarter moving average

Tech Bust & 9-11
Recession
Great Recession

?
Columbus CBSA Followed National Trends

Real Estate Returns Columbus vs. Nation
4 quarter moving average
Leverage has been favorable due to low interest rates.
Loan-to-Value for Institutional Real Estate

LTV relatively conservative for institutional investors
Price Level

CRE Slightly above Long-term Trend Line and Pre-Recession Peak
Real Estate Fund Contributions and Distributions
4Q Rolling Total as of December 31, 2015

Lots of capital
Q4’15 VOLUME HIT THE SAME RANGE AS 06’Q4 AND 07’Q1

US Quarterly Volume & Pricing

*Moody’s/RCA CPPI, national aggregate, December 2000 = 100
BUT US DEAL VOLUME TAKING A SPRING BREAK
RECORD CROSS-BORDER INFLOWS INTO US

US Direct Acquisitions by Foreign Buyers

- Canada
- Europe
- Middle East
- Latin America
- Asia
- Australia

Billions

Years: '05, '06, '07, '08, '09, '10, '11, '12, '13, '14, '15

Graph shows the foreign acquisitions into the US from selected regions over the years 2005 to 2015.
## 2015 DEAL VOLUME (EXCLUDING DEVELOPMENT SITES)

<table>
<thead>
<tr>
<th>Market</th>
<th>2015 Sales Volume ($M)</th>
<th>YOY Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>NYC Metro</td>
<td>$80,045</td>
<td>38%</td>
</tr>
<tr>
<td>London Metro</td>
<td>$57,048</td>
<td>29%</td>
</tr>
<tr>
<td>LA Metro</td>
<td>$36,340</td>
<td>26%</td>
</tr>
<tr>
<td>Tokyo</td>
<td>$32,816</td>
<td>-20%</td>
</tr>
<tr>
<td>SF Metro</td>
<td>$32,020</td>
<td>20%</td>
</tr>
<tr>
<td>Paris</td>
<td>$26,904</td>
<td>6%</td>
</tr>
<tr>
<td>DC Metro</td>
<td>$22,415</td>
<td>55%</td>
</tr>
<tr>
<td>Chicago</td>
<td>$19,882</td>
<td>48%</td>
</tr>
<tr>
<td>Dallas</td>
<td>$17,389</td>
<td>32%</td>
</tr>
<tr>
<td>Atlanta</td>
<td>$15,627</td>
<td>27%</td>
</tr>
<tr>
<td>Boston</td>
<td>$15,576</td>
<td>20%</td>
</tr>
<tr>
<td>Shanghai</td>
<td>$15,417</td>
<td>89%</td>
</tr>
<tr>
<td>So Fla</td>
<td>$14,248</td>
<td>33%</td>
</tr>
<tr>
<td>Seattle</td>
<td>$13,119</td>
<td>75%</td>
</tr>
<tr>
<td>Berlin-Brandenburg</td>
<td>$12,395</td>
<td>43%</td>
</tr>
<tr>
<td>Sydney</td>
<td>$11,828</td>
<td>-17%</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>$11,754</td>
<td>-13%</td>
</tr>
<tr>
<td>Phoenix</td>
<td>$10,779</td>
<td>65%</td>
</tr>
<tr>
<td>Rhine-Ruhr</td>
<td>$10,378</td>
<td>13%</td>
</tr>
<tr>
<td>Houston</td>
<td>$10,357</td>
<td>6%</td>
</tr>
<tr>
<td>Melbourne</td>
<td>$9,991</td>
<td>2%</td>
</tr>
<tr>
<td>Amsterdam/Randstad</td>
<td>$9,309</td>
<td>49%</td>
</tr>
<tr>
<td>Denver</td>
<td>$9,285</td>
<td>26%</td>
</tr>
<tr>
<td>Frankfurt/Rhine-Main</td>
<td>$9,157</td>
<td>9%</td>
</tr>
<tr>
<td>San Diego</td>
<td>$8,265</td>
<td>49%</td>
</tr>
<tr>
<td>Germany other</td>
<td>$8,216</td>
<td>-30%</td>
</tr>
<tr>
<td>Toronto</td>
<td>$7,304</td>
<td>13%</td>
</tr>
<tr>
<td>Austin</td>
<td>$7,223</td>
<td>15%</td>
</tr>
<tr>
<td>Sweden other</td>
<td>$6,968</td>
<td>3%</td>
</tr>
<tr>
<td>Philly Metro</td>
<td>$6,613</td>
<td>11%</td>
</tr>
</tbody>
</table>

US has 7 of Top 10 Cities Worldwide for Deal Volume
Foreign Buyers a Potential Structural Shift

Cross-Border Acquisitions of US Apartments

Canada
Europe
Middle East
Asia
Australia
Latin America

Lots of interest in apartments – perhaps late to the game.
Total NPI Returns by Property Type

Annual Returns Over Last Five Years

- Apartments best returns coming out of recession
- Industrial has taken the lead in returns.
NPI Annual Rental Income Growth by Property Type
*Period Ending Fourth Quarter 2015*

Although apartments still experiencing strong rent growth. May have been already been anticipated in returns.
2015 Year-End Summary: Space Market Observations

Quarterly Occupancy Rate

Rental Income Growth (4Q Rolling)

NOI Growth (4Q Rolling)

Cash Flow Growth (4QMA)

Fundamentals still good
NPI Rental Income Growth

Rent Growth
Driving Returns

Rolling Four Quarters

Rental Income Growth vs NPI (Rolling Four Quarters)
Cap Rate Compression also Helping to Drive Returns

But high spread to Treasuries (over 200 bp)
Yet starting to see warnings in headlines

**Will property prices continue to go up** in 2016? A Morgan Stanley report grabbed the industry’s attention recently when it **proclaimed that the U.S. commercial real estate universe will experience zero growth in prices** in the year ahead. Morgan Stanley researchers reasoned it was unlikely net operating incomes (NOIs) would continue rising at the pace needed to guarantee price growth in an environment of economic uncertainty. (They did point out there would be bifurcation in price appreciation between best and worst assets and certain geographic markets).
Top News

Analysts expect market correction for commercial property

Office space in Houston and high-end condos in Manhattan are two areas where some experts see a looming downturn that could lead to defaults. Kenneth Riggs, president of real estate research firm Situs RERC, expects a market correction but says it will be "manageable." The Wall Street Journal (tiered subscription model) (3/8)

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Index shows 0.3% decline in commercial property prices

The Moody's/RCA Commercial Property Price Index dropped 0.3% in January from the previous month, the first time it has fallen since 2010. Office and industrial buildings each had a price decline of more than 1%. "This is a significant milestone that signals that a shift in sentiment among commercial-property investors is under way," Moody's Investors Service said. Bloomberg (3/7)

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Apartment REITs: Rent Growth Slowing

According to the latest report from investment bank Cohen & Co., notable transitions to deceleration on a T12M basis... Read More

Apartment Markets Mixed in the April NMHC Quarterly Survey

Construction financing less available
Industry News

CalPERS to ramp up real estate development
IPE Real Estate - April 14, 2016
The California Public Employees Retirement System (CalPERS) is considering ramping up its real estate development activity as the availability of existing core assets continues to dwindle.

Calstrs Selling U.S. Real Estate While Buying European Assets
Bloomberg - April 13, 2016
The $180 billion California State Teachers' Retirement System is buying more equities and real estate in Europe while selling U.S. properties, which are "priced to perfection," according to the fund's chief investment officer.

Sam Zell says US economy "doing pretty well," but cycle "in the ninth inning"
The Real Deal - April 13, 2016
Equity Residential chair riffs on Starwood deal, election and millennials' mating habits at NYU REIT conference.
FIRST MONTHLY DECLINE IN PRICES IN 6 YEARS: FEB TOO

Moody’s/RCA Commercial Property Price Indices

RCA tracks transactions over $2.5 million
Returns have been dropping – but back to long term average
Columbus CBSA
Total Return (Unleveraged)

Columbus also down 1st quarter of 2016 although still quite strong for past four quarters.

Approx. $750 billion
Institutional Investors and Plan Sponsors expect returns to continue to drop through 2019.
LOAN ORIGINATIONS IN ‘06 & ‘07 WHAT HAPPENS IN ’16 & ‘17?

Key Property Sectors, Office, Industrial, Retail, Apartment

$ Billions


CMBS  Non-CMBS
HEADWIND: UPCOMING WAVE OF MATURITIES/OPPORTUNITIES

Refinancing the 2006 and 2007 Originations

Due to tighter lending standards, many loans will require more equity when refinanced.

Outlook under Baseline Moody’s Forecast of RCA Market CPPI’s
Columbus vs. Nation
Last 5 quarters

Columbus
National

15-1
15-2
15-3
15-4
16-1
Total NPI Returns: Top 10 Markets by Market Value

Top 10 Markets versus Other Markets

Capital has been moving beyond the top 10 markets

<table>
<thead>
<tr>
<th>Top 10 Markets</th>
<th>MV ($Bil)</th>
</tr>
</thead>
<tbody>
<tr>
<td>New York City</td>
<td>$51.80</td>
</tr>
<tr>
<td>Washington DC</td>
<td>$40.10</td>
</tr>
<tr>
<td>Los Angeles</td>
<td>$37.32</td>
</tr>
<tr>
<td>Chicago</td>
<td>$29.89</td>
</tr>
<tr>
<td>San Francisco</td>
<td>$23.77</td>
</tr>
<tr>
<td>Seattle</td>
<td>$20.30</td>
</tr>
<tr>
<td>Houston</td>
<td>$19.93</td>
</tr>
<tr>
<td>Dallas</td>
<td>$18.21</td>
</tr>
<tr>
<td>Boston</td>
<td>$16.26</td>
</tr>
<tr>
<td>Riverside</td>
<td>$12.39</td>
</tr>
</tbody>
</table>

Top 10 Markets and NPI

Columbus here 4th qtr of 2015
“From Great to Good”

• Despite edging lower over the past 5 quarters, total returns remain healthy relative to long term averages.

• CRE remains a strong relative performer across asset classes, supporting capital flows into the sector

• Low interest rates in US and globally keep cap rates at historic lows

• NOI growth has slowed but still above historic average

• Occupancy can’t get much higher – always “frictional vacancy”

• May be in the 9th inning but likely to go into some “extra innings.”

• Money still talks – but nervous about current price levels.