

The Real Estate Roundtable Sentiment Index



Third Quarter 2022



The Real Estate Roundtable

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The Real Estate Roundtable is pleased to announce the results from the Q3 2022 Real Estate Roundtable Sentiment Survey. The quarterly survey is the commercial real estate industry's comprehensive measure of senior executives' confidence and expectations about the commercial real estate market environment. Conducted by Ferguson Partners on behalf of The Roundtable, it measures the views of CEOs, presidents, and other top commercial real estate industry executives regarding current conditions and the future outlook on three topics:

1. Overall real estate conditions
 2. Access to capital markets
 3. Real estate asset values
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Topline Findings

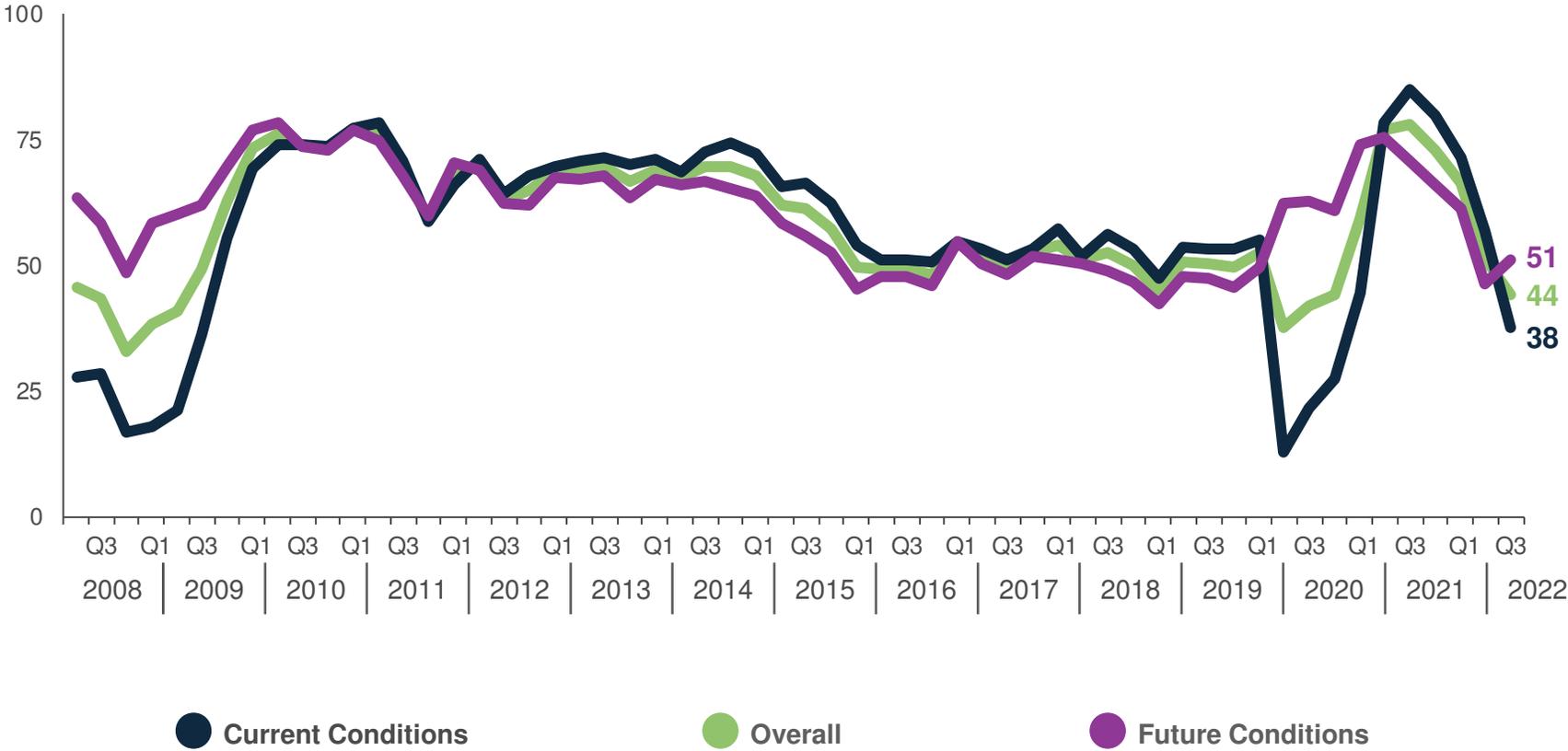
- The Q3 2022 Real Estate Roundtable Sentiment Index registered an overall score of 44, a decrease of 7 points from the previous quarter's overall score and 34 points lower than a year earlier. Survey respondents are cautious of rising interest rates, increased inflation, supply chain disruptions, and other issues but remain optimistic regarding the underlying fundamentals for real estate.
- While fundamentals, such as industrial and multifamily, remain strong in terms of supply and demand, there is concern over current market conditions for other asset classes, particularly office and retail.
- Although in the short-term the pandemic has led to a lack of enthusiasm for office and retail assets, industry leaders expect strong, long-term demand for assets that allow increased flexibility by providing tenants with more amenities and higher quality accommodations. Rising interest rates and general market uncertainty represent clear challenges facing asset pricing; where trades are taking place, they have been occurring at a discount relative to recent high-water marks.
- In terms of capital markets, participants noted that capital is available, though market uncertainty has induced hesitancy for risk-taking and tightening across both debt and equity.

¹ The Real Estate Roundtable Sentiment Index is measured on a scale of 1–100. It is the average of The Real Estate Roundtable Future Index and The Real Estate Roundtable Current Index. To register an Index of 100, all respondents would have to answer that they believe conditions are “much better” today than one year ago and will be “much better” one year from now.



Exhibit 1

The Real Estate Roundtable Sentiment Index



General Conditions

The Q3 2022 Real Estate Roundtable Sentiment Index registered an overall score of 44, a decrease of 7 points from the previous quarter's overall score and 34 points lower than a year earlier. Survey respondents are cautious of rising interest rates, increased inflation, supply chain disruptions, and other issues but remain optimistic regarding the underlying fundamentals for real estate.

“Institutional quality real estate is doing much better than most conventional asset classes - just look at the public equities markets and the turmoil there especially in the technology sector. I think there is a floor to real estate demand, and we believe this is not a depression or major repricing; this is just a softening/reversion to the mean.”

“We are still seeing strong rental rate growth and record high tenant retention, but something is going to have to give with rising rates. People are trying to remain debt neutral but there were a lot of deals that were underwritten aggressively the last few years with low cap rates that may not work anymore.”

“One of the biggest challenges facing the real estate industry is a broader macro challenge of lack of labor supply in the U.S. We need more workers. Not just in offices but in all the things that keep our economy humming: restaurants, hotels, logistics, etc. All these areas support the underlying fundamentals of our business.”

“There is a big issue of supply chain and labor market tightness that makes new development challenging, even when you have a contract signed. Material costs have skyrocketed due to the lack of materials and labor shortages.”

“The biggest concern right now is the rise in interest rates. There should be a direct correlation where valuations will decrease because the cost of capital is more expensive.”

“With supply chain disruptions, a geopolitical conflict, and the Fed's reaction, there is massive uncertainty around inflation, and where the economy is heading. Depending on where you look you can get mixed signals. Investors tend not to like uncertainty, so a lot of people are sitting on their hands until things become clearer.”

“The market has changed massively since the last quarter. Risk free rates are up significantly, which means that the way things have been trading, deals aren't going to pencil out anymore. The result is prices comes down.”

General Conditions (continued)

While fundamentals, such as industrial and multifamily, remain strong in terms of supply and demand, there is concern over current market conditions for other asset classes, particularly office and retail.

“As long-term investors, we remain optimistic on the underlying real estate fundamentals, especially in ‘needs based real estate’ such as housing. Residential in many different forms is still doing well because of the housing shortage. Almost every residential market is back to pre-Covid rental pricing.”

“Office is very nuanced. New stock, with light and airy atmospheres, and efficient buildings are coveted. The older and vintage buildings have dwindling occupancy and declining rental rates. The pandemic accelerated flexibility and disinterest in going into some of those older spaces.”

“Hospitality properties that are designed to allow consumers to live, work, and play in different ways are in demand.”

“Retail is still a big unknown – we don’t know which tenants are going to stay in a brick-and-mortar store. The internet and Covid-19 has just accelerated this uncertainty. There is not a lot of appetite for it.”

“With industrial, the darling asset class, there’s some chatter that valuations are topping. The fundamental demand drivers of e-commerce may be slowing, heightening rates, supply chain issues, etc. are all percolating to more conservative underwriting but the long-term runway for the asset class isn’t changing.”

“Life sciences may be in some trouble because it’s an undercapitalized sector. We’re bullish on it, but as with other areas, there’s a problem where people tend to overbuild which may bring some short-term pain.”

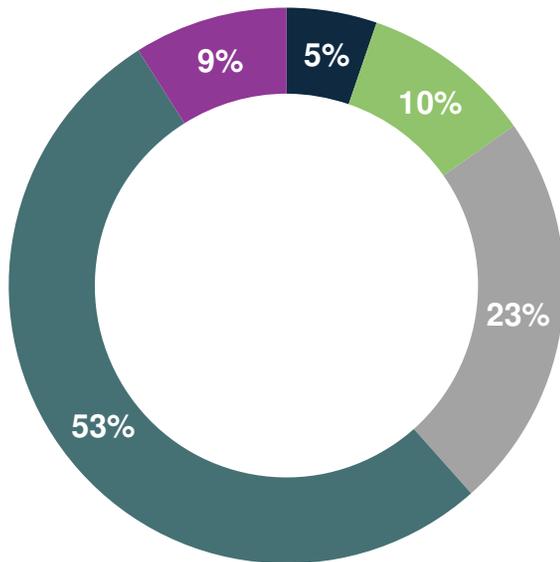
Exhibit 2

General Market Conditions

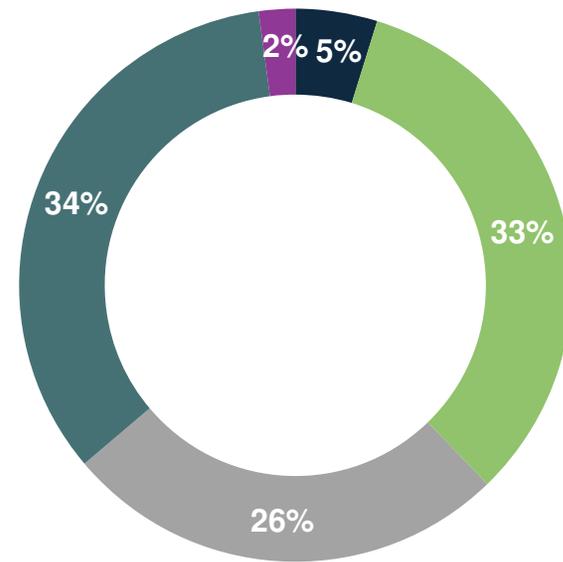
% of respondents

- Much better
- Somewhat better
- About the same
- Somewhat worse
- Much worse

Today vs. One Year Ago



One Year From Now vs. Today



Asset Values

Although in the short-term the pandemic has led to a lack of enthusiasm for office and retail assets, industry leaders expect strong, long-term demand for assets that allow increased flexibility by providing tenants with more amenities and higher quality accommodations. Rising interest rates and general market uncertainty represent clear challenges facing asset pricing; where trades are taking place, they have been occurring at a discount relative to recent high-water marks.

“ Asset prices have reflected the interest rate movement. When interest rates are up, asset prices are down.”

“ Values are down across the board in every asset class. It’s difficult to finance right now due to the widened spread and in six month’s time, it’s going to be worse than today.”

“ Investors are turning into vultures overnight, but there aren’t a ton of bargains out there yet. Everyone is afraid to buy something because they’re fearing it’s too high. Investors are trying to steal assets, not trying to look if it’s a good deal. There is not a whole lot of movement right now.”

“ Private market pricing is as wide as it has ever been. Private cap rates are moving up, but there’s 150 bps in differentiation between the two.”

“ Underwriting has gotten more conservative with firms looking to de-risk which is rippling through availability and pricing. It depends on the asset class, but right now assets are trading at about 5% less for multifamily and 10 – 20% less for a well-leased office building. Even in the best asset class, prices are down 5 – 10% from six months ago.”

“ The office sector continues to see an erosion in asset valuation due to poor lease ups. The high interest rates and lack of availability of debt capital are creating additional challenges, meaning office values have come in 15 – 30% below where they were over the past few quarters.”

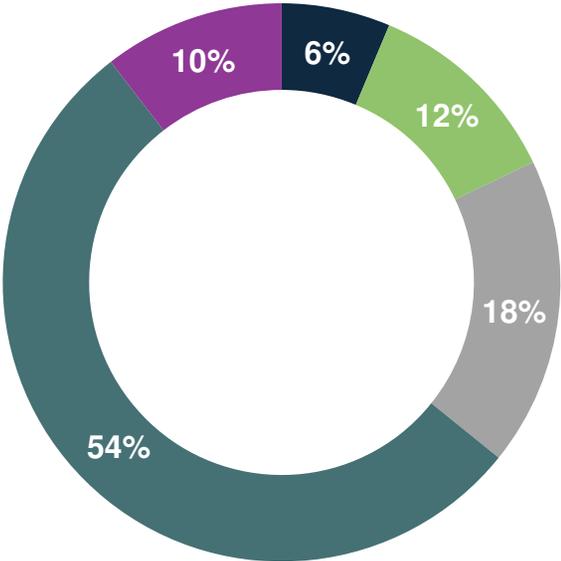
Exhibit 3

Real Estate Asset Values

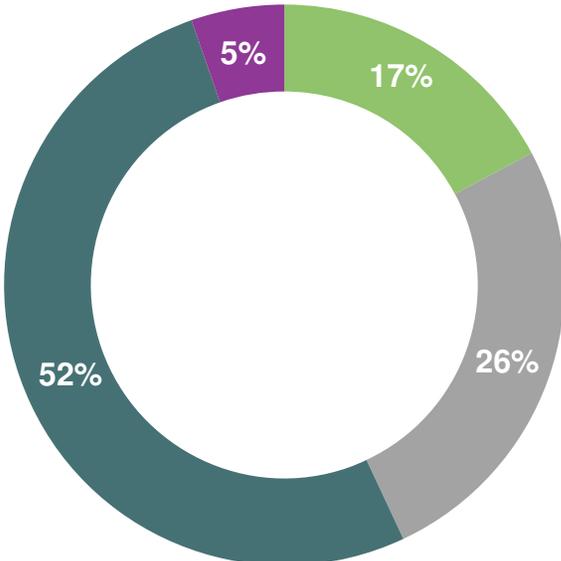
% of respondents

- Much higher
- Somewhat higher
- About the same
- Somewhat lower
- Much lower

Today vs. One Year Ago



One Year From Now vs. Today



Capital Markets

In terms of capital markets, participants noted that capital is available, though market uncertainty has induced hesitancy for risk-taking and tightening across both debt and equity.

“Domestic institutions are running up against the denominator effect where they don't have as much capital for their real estate portfolio because their portfolio has been affected by the equity markets. Some are looking to sell assets to get liquidity.”

“Debt is available, it's just more expensive. People got really used to cheap money and are being forced to recalibrate a little bit.”

“There's still a tremendous amount of equity available in real estate. However, most of that equity isn't in a position to move yet given current market conditions and the related uncertainty. Most practitioners are looking at a big shift from non-traditional debt lenders because of the huge decrease in debt availability.”

“For equity capital, there's still a lot of appetite. The strong demand and abundance of equity will continue through the year; however, people are waiting because no one wants to be the one to take the risk. In particular, sovereign wealth funds and pension funds are trying to determine what the new pricing and equity model looks like.”

“The public debt market is available, but it adjusted due to the price spread and the current high rates. The private debt market took a little while to react, but now prices are closer to the public market.”

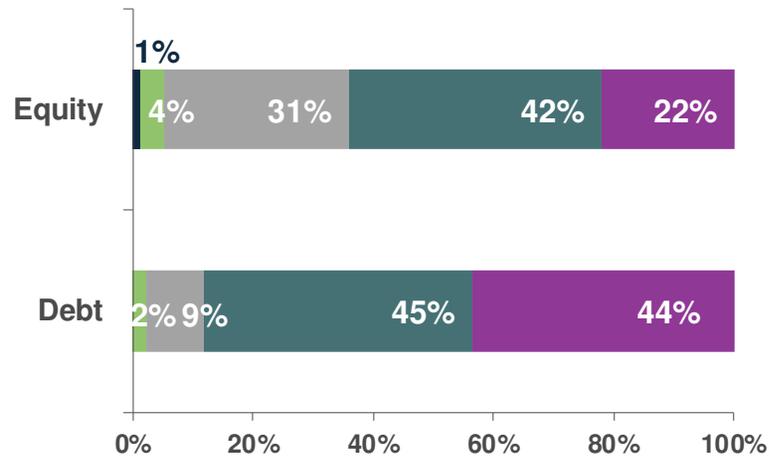
Exhibit 4

Availability of Capital

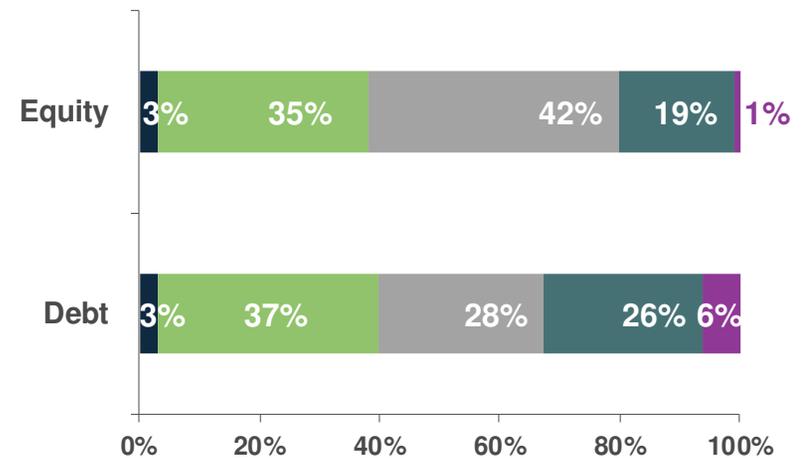
% of respondents

- Much better
- Somewhat better
- About the same
- Somewhat worse
- Much worse

Today vs. One Year Ago



One Year From Now vs. Today



Participants

(Please note that this is only a partial list. Not all survey participants elected to be listed.)

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