Third Quarter 2023

The Real Estate Roundtable Sentiment Index

Ferguson Partners

The Real Estate Roundtable

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The Real Estate Roundtable is pleased to announce the results from the Q3 2023 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:

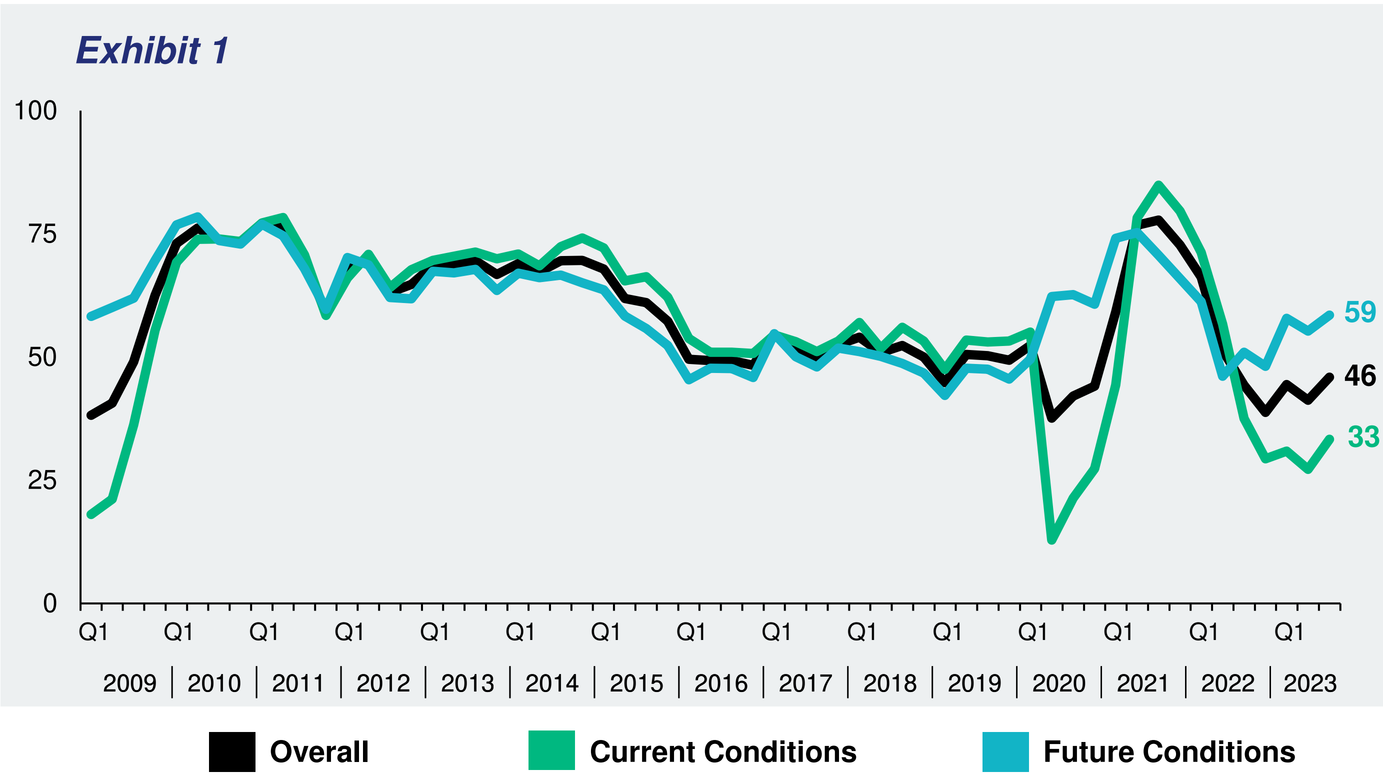
1. Overall real estate conditions
2. Access to capital markets
3. Real estate asset values

Topline Findings

- The Q3 2023 Real Estate Roundtable Sentiment Index registered an overall score of 46, an increase of five points from the previous quarter. The Current Index registered 33, a six-point increase from Q2 2023, and the Future Index posted a score of 59 points, an increase of four points from the previous quarter.
- Disparities between asset classes persist in these challenging market conditions. Hotel and retail markets are largely performing well. Niche asset classes continue to generate interest. On the other hand, office is performing poorly, and rental growth in multifamily and industrial are starting to abate.
- Perceptions of declining asset values continue to dominate, with 95% of survey participants reporting that asset values are lower as compared to last year. While Class A properties across all asset classes are trading at competitive prices, managers are still in a "wait and see" mindset for other assets, resulting in lower transaction volumes and an inability to complete accurate valuations.
- The availability of capital continues to be a pressing topic in regards to both debt and equity; 85% and 69% of survey participants, respectively, believe that today's conditions are more difficult than a year ago. Although managers face a difficult capital raising environment, only 24% and 9% of participants believe debt and equity availability respectively will be worse a year from now as the industry works to creatively solve financing issues.

[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.

The Real Estate Roundtable Sentiment Index



- In the Q3 RER Sentiment Survey, participants rated the overall market conditions as a score of 46, current conditions as 33, and future conditions as 59
- Compared to one year ago, sentiments of current conditions are down by 5 points, perceptions of future conditions are up by 8 points, and overall conditions are up by 2 points
- In comparison to last quarter, sentiments on current conditions are up by 6 points, perceptions of future conditions are up by 4 points, and overall conditions are up by 5 points

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General Conditions

The Q3 2023 Real Estate Roundtable Sentiment Index registered an overall score of 46, an increase of five points from the previous quarter. The Current Index registered a 33, a six-point increase from Q2 2023, and the Future Index posted a score of 59 points, an increase of four points from the previous quarter.

“For our credit funds, business has never been better. Traditional lenders are either doing significantly less volume or have exited the space entirely. Frankly, the risk-adjusted return for credit is outstanding right now compared to equity investments.”

“This is going to be an event-driven market. The current landscape involves elements of price discovery and limited capital availability, resulting in a stalemate. When loans mature or equity recalibrates its interest in commercial real estate, we can expect more movement.”

“Despite doing well at the asset level, interest rates are causing balance sheet stress even for non-office sectors. This is particularly true in situations where loans are maturing and an owner needs to refinance, or for those with floating rate loans.”

“Insurance, taxes, and labor put pressure on the bottom line across managed and owned portfolios. Insurance especially is a rising cost. We’re seeing a massive rise in year-over-year premiums, which of course has an impact on underwriting.”

“The industry continues to grapple with labor costs, which pose challenges for development projects. In cases where financing costs do not align with cap rates, those projects are being postponed or tabled.”

“With the slowdown in transactions, there has been a renewed emphasis on asset management and maximizing returns on owned assets. We haven’t had staffing cuts, but we’re slowing down headcount growth.”

“It feels like real estate is in a recession, and it was led there by interest rate hikes. Nobody can transact, and we have a wall of debt maturities coming.”

General Conditions (continued)

Disparities between asset classes persist in these challenging market conditions. Hotel and retail markets are largely performing well. Niche asset classes continue to generate interest. On the other hand, office is performing poorly, and rental growth in multifamily and industrial are starting to abate.

> Single-family rental has fared better than multifamily or manufactured housing. Multifamily rents are abating a little, but demand is still healthy for single-family rental properties."

> Hospitality can absorb higher interest rates because they can reprice on a nightly basis. As an asset class, it also tends to trade at higher cap rates, and we haven't seen any downward price adjustments for quality assets."

> We can't get enough of last-mile industrial, but there's some cooling in rent growth even there. The assets are healthy, but the valuations are off."

> Office has been deeply damaged. The loans due in the next year and a half are mostly for office properties, and most of those are significantly down in value. There are a lot of keys being handed back, and some extraordinary buildings that are selling."

> In senior living and healthcare, you can't get bank financing for anything. We aren't done with price discovery in healthcare, and we've seen potential deals getting pulled off the market."

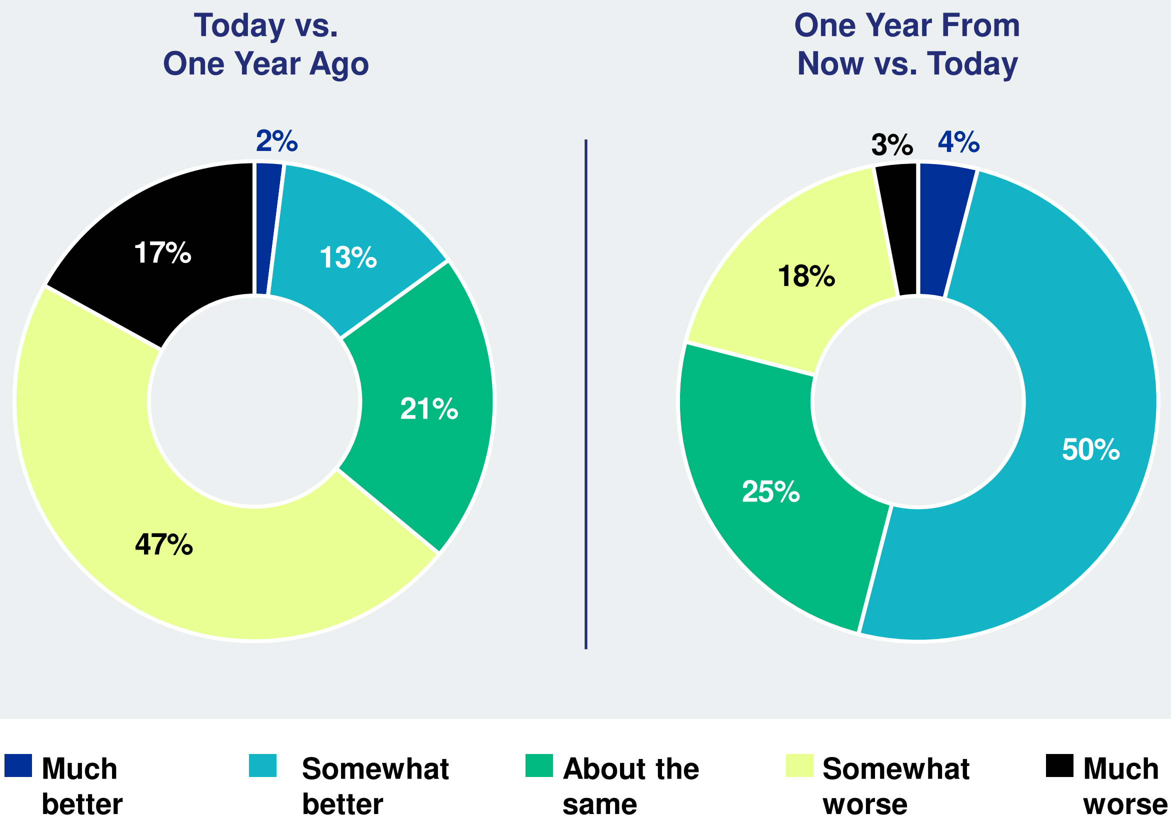
> Land presents unique challenges due to various factors such as high interest rates, escalating construction costs, and elevated exit cap rates."

> Retail, including malls, continues to exhibit strong fundamentals with foot traffic, sales, and leasing velocity. The retail asset class has demonstrated resilience, particularly as the industry gets creative with re-developing components of properties and adding recreational businesses to former big-box spaces."

General Market Conditions

% of respondents

Exhibit 2



- Regarding sentiment on current market conditions, 64% believe it is a less favorable environment compared to one year ago, 15% feel it has improved, and 21% believe conditions remain the same
- Hindsight is 20/20, with only 36% of participants in the Q3 2022 RER Sentiment Survey believing that general market conditions would be worse in Q3 2023
- Looking towards the future, 54% of participants believe that a year from now will present more favorable market conditions

Asset Values

Perceptions of declining asset values continue to dominate, with 95% of survey participants reporting that asset values are lower as compared to last year. While Class A properties across all asset classes are trading at competitive prices, managers are still in a "wait and see" mindset for other assets, resulting in lower transaction volumes and an inability to complete accurate valuations.

> "With transactions extremely slow, there are not enough comparable properties to price assets. With no rear-view mirror, devaluations are slowly being recognized and realized."

> "If you aren't forced to sell, you're not selling, and if you're buying, you're looking for a really good deal. That leads to transaction volumes down from last year."

> "For quality assets, there have been little downward price adjustments."

> "Managers who have capital and an interest in acquiring assets hold a significant advantage, allowing them to negotiate and price assets down aggressively."

> "Strong assets are trading at very aggressive cap rates and are priced to perfection. Assets with a limited growth profile are trading in a low cap rate range."

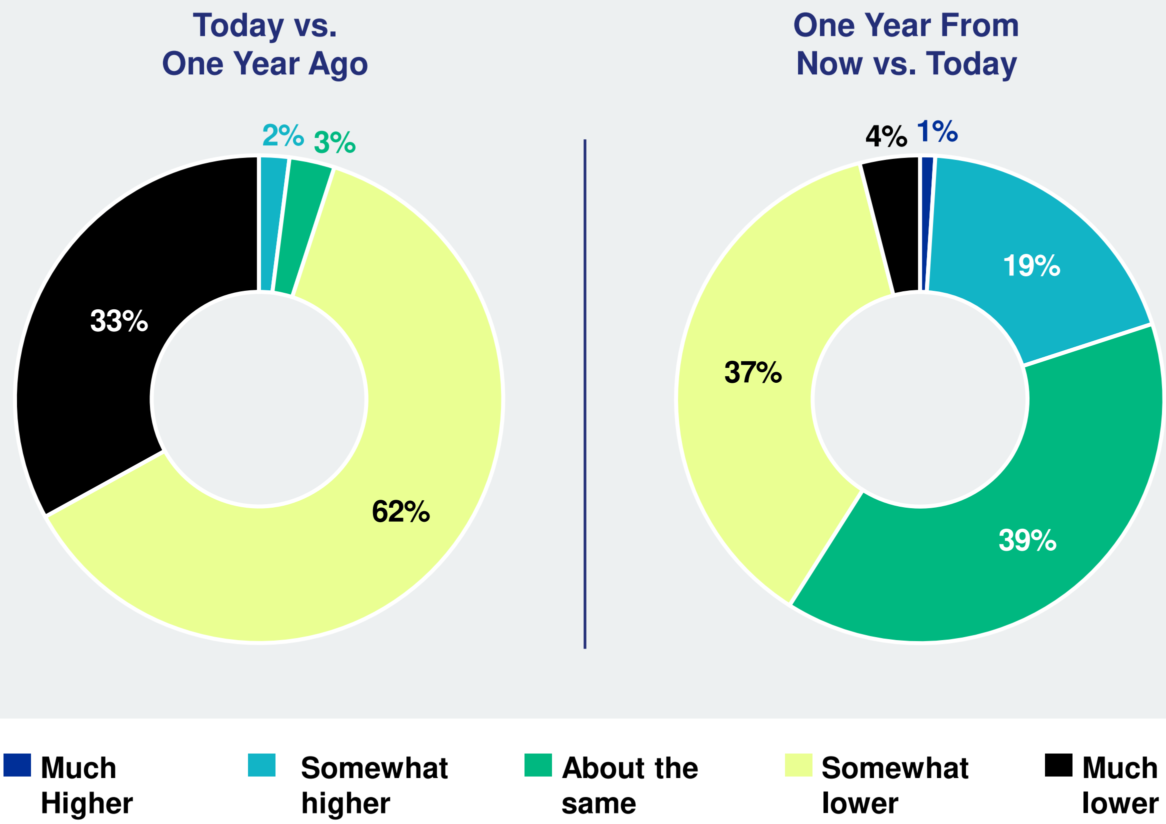
> "The transaction market has witnessed a significant decline of 75% compared to last year. It is likely that the market will remain in a price discovery phase until the Federal Reserve ceases its interest rate hiking."

> "Those that have capital are not investing right now because values are not tantalizing enough to investors. Instead, firms are focusing on transactions that make use of creative financing structures through preferred equities and debt, where they can protect against uncertain valuations."

Real Estate Asset Values

% of respondents

Exhibit 3



- Regarding sentiment on the state of current asset values, 95% believe they are lower than one year ago, 2% feel they are higher, and 3% believe asset values have remained the same compared to a year ago
- This contrasts with the Q3 2022 RER Sentiment Survey where only 57% of participants believed that asset values would be lower in Q3 2023, indicating a steep decline in perceptions on asset values
- Looking towards the future, only 20% of participants believe that a year from now will present more favorable asset values

Capital Markets

The availability of capital continues to be a pressing topic in regards to both debt and equity; 85% and 69% of survey participants, respectively, believe that today's conditions are more difficult than a year ago. Although managers face a difficult capital raising environment, only 24% and 9% of participants believe debt and equity availability respectively will be worse a year from now as the industry works to creatively solve financing issues.

“Over the past 15 months, there has been a significant drying up of debt capital in the market. Regional banks, which typically drive 40% of the debt markets, have shifted their focus towards building up their reserves and are not actively lending. As a result, the spreads between borrowing and lending rates have widened considerably, reaching enormous levels.”

“When public pensions and sovereign wealth funds invest, the tides rise. Currently, however, the tide is going out because a lot of funds are overallocated to private assets. As a result, these equity capital sources will be selective.”

“With a disparity in equity and debt availability, there is significant international interest in private credit opportunities within the United States. Of course, the level of interest may vary depending on the specific market and asset class, but there is a lot of foreign demand expected for US investments.”

“Equity finds itself in a precarious position. While original equity positions were strong, reduced cash flow available to support debt and refinancing rates have resulted in negative equity returns. Not to mention, new equity capital faces return hurdles that are 4-6% higher than the equity deployed over the past 36 months.”

“The debt capital is there, it's just 200-300 bps more than a few years ago.”

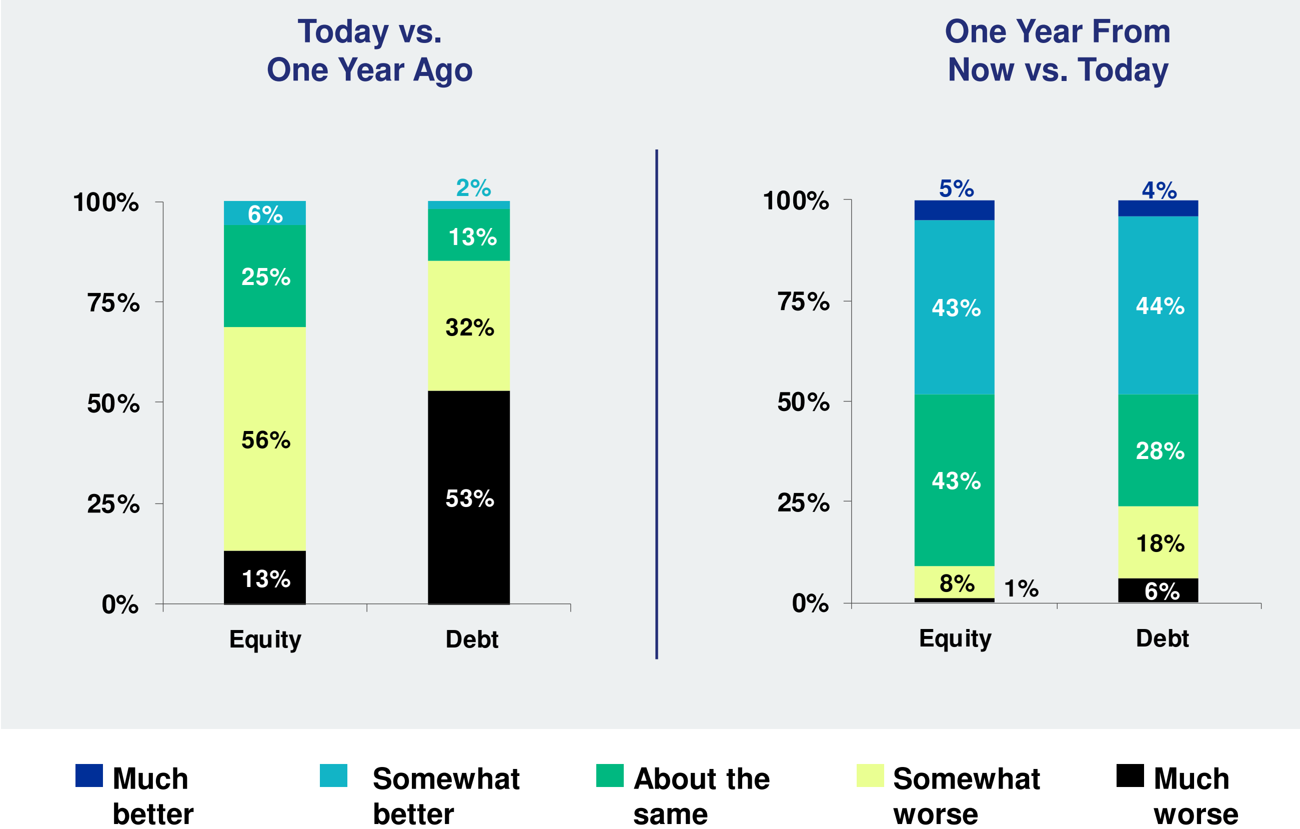
“We're in a capital markets disarray, resulting in two things. First, there's a significant need to revalue and reprice all real estate that doesn't have in-place, long-term fixed rate financing. Secondly, transaction volume is extremely slow. This leads to a disconnect between strong underlying fundamentals and an unknown evaluation cycle driven by high interest rates.”

“This is the most difficult fundraising environment in the past 20 years.”

Availability of Capital

% of respondents

Exhibit 4



- Regarding sentiment on the availability of equity capital, 69% believe it is worse compared to one year ago, 6% feel it has improved, and 25% believe the availability of equity remains the same
- In terms of the availability of debt capital, 85% of participants believe it is worse compared to one year ago, 2% feel it has improved, and 13% believe the availability of debt remains the same
- Looking towards the future, 48% of participants believe that equity and debt availability will be better one year from now, and 9% and 24% of participants believe that equity and debt availability respectively will be worse one year from now

Participants

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

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Ferguson Partners Consulting – Who we are

We are problem solvers for the real assets industries helping our clients with the strategy, structure, and performance of their businesses, often at times of transition and transformation. Our service offerings include:

- **Strategy & Market Positioning –** Optimizing business strategy to compete in the market
- **Organizational Design –** Getting the right structure, roles, and people in place to execute the business plan
- **Governance & Succession Planning –** Planning around current and future leadership, ownership, governance, and decision making
- **Operational Efficiency –** Ensuring the performance of the business is optimized through rigorous assessments and benchmarking of staffing and financial results

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