Fourth 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 Q4 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

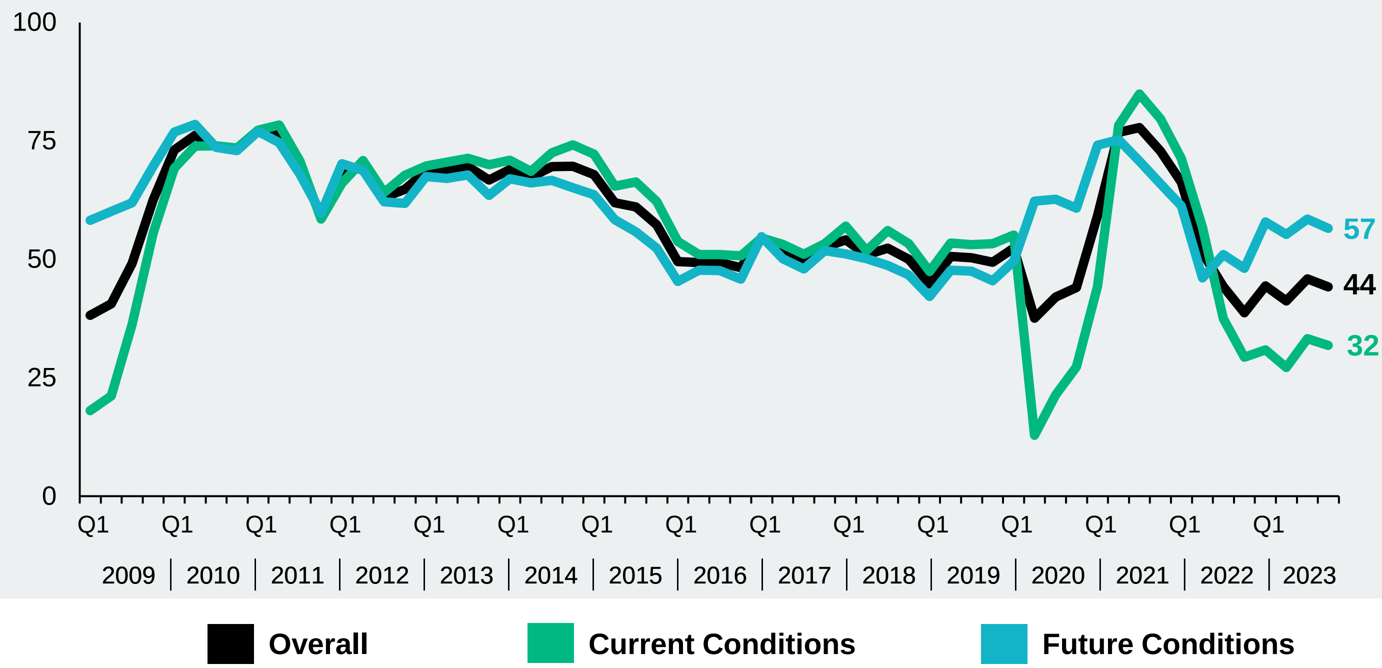
Topline Findings

- The Q4 2023 Real Estate Roundtable Sentiment Index registered an overall score of 44, a decrease of two points from the previous quarter. The Current Index registered 32, a one-point decrease from Q3 2023, and the Future Index posted a score of 57 points, a decrease of two points from the previous quarter. These stable indices highlight the persistent challenges faced by participants in the real estate market.
- Although there are variations among asset classes and even within specific property types, ongoing uncertainty within the broader commercial real estate industry persists due to concerns about liquidity, capital availability, interest rates, and remote work. Bright spots exist in smaller classes, such as data centers, outlet malls, and hotels, while multifamily and industrial continue to attract interest. Within the office sector, class A properties with top-of-the-line amenities are the lone high performers.
- An overwhelming 92% of survey participants indicate that asset values have decreased compared to the previous year. The valuation process has been challenging due to limited transactions, and the combination of current cap rates and fluctuating interest rates has further complicated pricing, ultimately leading to a view that asset values have decreased relative to one year ago.
- Survey participants express ongoing concerns about the capital markets landscape, with 70% indicating that the availability of equity capital has worsened compared to a year ago, and 86% believing the availability of debt capital is also worse.

[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

Exhibit 1



- In the Q4 RER Sentiment Survey, participants rated the overall market conditions as a score of 44, current conditions as 32, and future conditions as 57
- Compared to one year ago, sentiments of current conditions are up by 3 points, perceptions of future conditions are up by 9 points, and overall conditions are up by 5 points
- In comparison to last quarter, sentiments on current conditions are down by 1 point, perceptions of future conditions are down by 2 points, and overall conditions are down by 2 points

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General Conditions

The Q4 2023 Real Estate Roundtable Sentiment Index registered an overall score of 44, a decrease of two points from the previous quarter. The Current Index registered 32, a one-point decrease from Q3 2023, and the Future Index posted a score of 57 points, a decrease of two points from the previous quarter. These stable indices highlight the persistent challenges faced by participants in the real estate market.

“We’re experiencing a cost of capital crisis, not a demand driven boom-bust. When you examine real estate fundamentals, it is fairly healthy across almost every asset class, even though rents may be decelerating.”

“There’s a lot to be said about the emerging markets domestically in the U.S. As cities become less densely populated and second-tier markets experience increased population growth, there are a number of ‘new Nashvilles’ that the real estate market can capitalize on.”

“Insurance costs are steadily rising due to climate risk, which eats into profitability. However, this is the moment for managers to incorporate ESG considerations into deals, adopting a more active and assertive approach for their capital.”

“It’s hard to identify transaction opportunities, so we are focusing on our existing portfolio where we can control operations.”

“Right now, capital markets are driven by maturities and debt. At some point, investors will either start to commit more dollars or managers will hand the keys back to the banks.”

“On a positive note, managers are remaining calm and thoughtful fiduciaries to their investors. Senior-level executives are helping their younger colleagues who have never experienced distress in the markets.”

“As the focus moves away from core real estate, there’s a question about the value-added managers who profit from selling core assets. Who is going to buy these newly renovated core buildings? In the end, everything is going to need repricing.”

General Conditions (continued)

Although there are variations among asset classes and even within specific property types, ongoing uncertainty within the broader commercial real estate industry persists due to concerns about liquidity, capital availability, interest rates, and remote work. Bright spots exist in smaller classes, such as data centers, outlet malls, and hotels, while multifamily and industrial continue to attract interest. Within the office sector, class A properties with top-of-the-line amenities are the lone high performers.

“Your perspective depends on what assets you hold and the strength of your balance sheet. For those organizations with low leveraged assets, this is the best buying opportunity in over a decade. But for firms with lots of floating rate debt or office properties, it’s a bit trickier right now.”

“The average U.S. consumer is looking for reputable brands, but at reasonable prices. To address these consumer trends, there is healthy demand for brick-and-mortar outlet malls because they have relatively low rents and installation costs.”

“Although office assets are not performing well across the board, quality properties can outperform expectations. Office buildings aren’t going to disappear completely.”

“Three to four months ago, some asset classes like industrial, multifamily, and class A office, had stronger liquidity than others. Over the last three to four months, however, all asset classes are trending negatively and showing signs that they’re becoming difficult to transact.”

“Data centers are having their moment in the sun. Regardless of the increased attention to AI, landlords have increased pricing power because the largest service providers need data centers.”

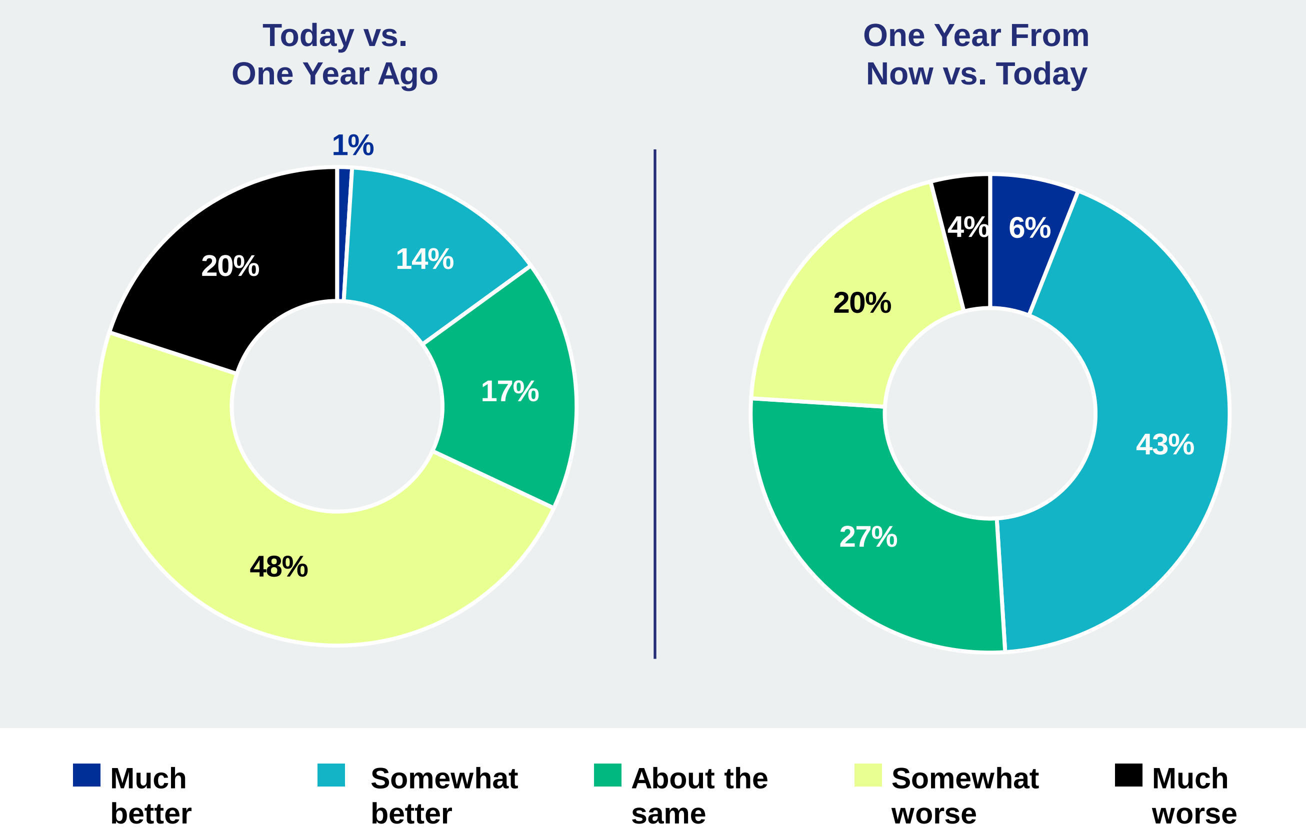
“The demand for apartments is still strong, but high construction costs and interest rates are discouraging builders. On top of real estate taxes and government intervention, multifamily development has started slowing.”

“Hotels are making a resurgence. Upper scale hotels can charge high rates to balance the lack of occupancy.”

General Market Conditions

% of respondents

Exhibit 2



- Regarding sentiment on current market conditions, 68% believe it is a less favorable environment compared to one year ago, 15% feel it has improved, and 17% believe conditions remain the same
- Hindsight is 20/20, with only 36% of participants in the Q4 2022 RER Sentiment Survey believing that general market conditions would be worse in Q4 2023
- Looking towards the future, 49% of participants believe that a year from now will present more favorable market conditions

Asset Values

An overwhelming 92% of survey participants indicate that asset values have decreased compared to the previous year. The valuation process has been challenging due to limited transactions, and the combination of current cap rates and fluctuating interest rates has further complicated pricing, ultimately leading to a view that asset values have decreased relative to one year ago.

> Asset values are solely dependent on the asset type and location. As a general observation, asset pricing is lower than it was six months ago, and I predict that it'll be lower six months from now than it is today. Pricing is down and will continue to decrease as long as interest rates remain high."

> Pricing assets is almost an impossible task [right now]. Valuations have decreased by around 20% compared to earlier this year, which is heavily influenced by current cap rates."

> Asset values are currently undergoing a reset to align with the prevailing higher interest rate environment, but this process may take some time due to the notable lag in transaction volume. Achieving market stability necessitates both stable interest rates and a predictable interest rate forecast."

> Spreads have widened quite substantially, even in multifamily and logistics. This is due to the lack of debt financing and the necessary equity returns. Where multifamily and industrial is pricing in the low 5s, the values are probably down 25% from their peak."

> There will be a 'great revaluation' cycle with more real estate assets priced lower. There haven't been enough transactions to collect good data, and the transactions that are happening are in the most dire of circumstances, which is driving erratic and less reliable market information. Hopefully, we will see more movement in 2024."

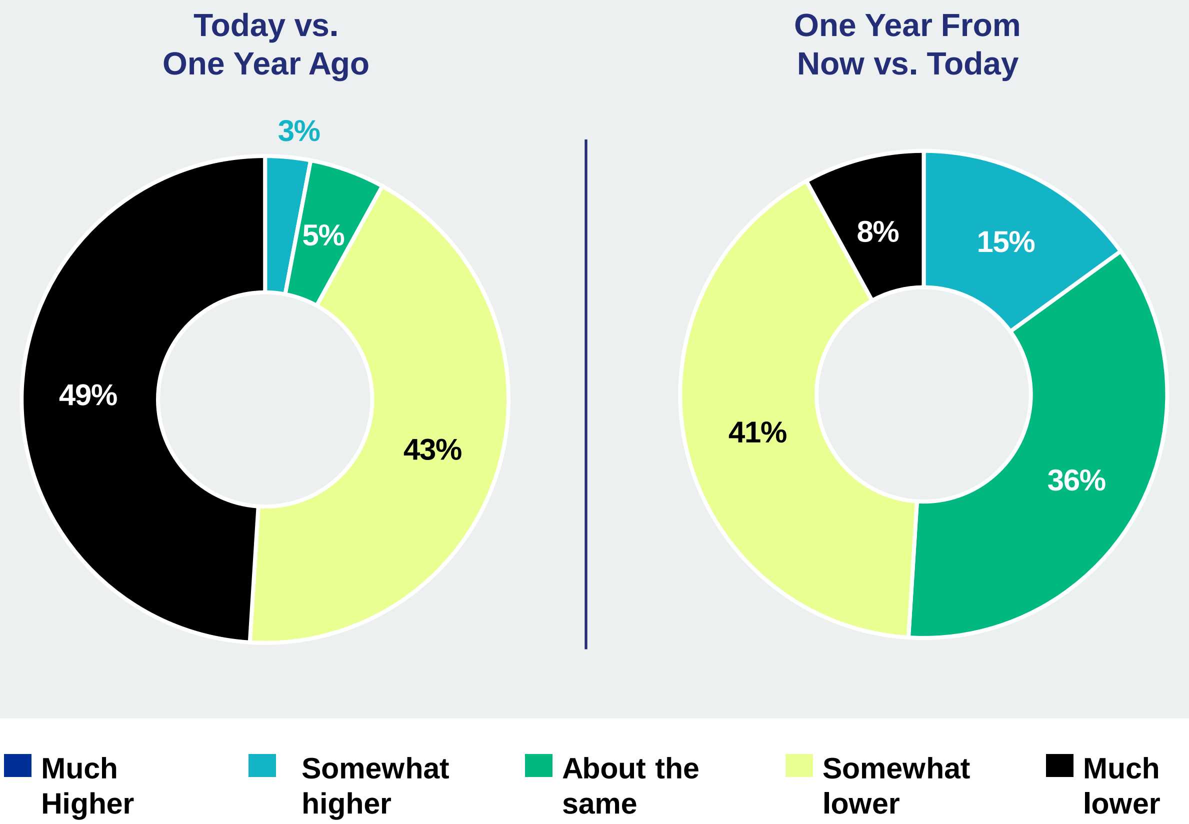
> Everything is priced 20% less, except for office. Office properties have unknown values in today's market."

> We've seen some downward pressure on valuations which will continue for the next 2-3 quarters. There may be some stabilization after that, but there will still be weaknesses over the next couple of quarters, with some asset classes experiencing it more harshly than others."

Real Estate Asset Values

% of respondents

Exhibit 3



- Regarding sentiment on the state of current asset values, 92% believe they are lower than one year ago, 3% feel they are higher, and 5% believe asset values have remained the same compared to a year ago
- This contrasts with the Q4 2022 RER Sentiment Survey where only 59% of participants believed that asset values would be lower in Q4 2023, indicating a steep decline in perceptions on asset values
- Looking towards the future, only 15% of participants believe that a year from now will present more favorable asset values

Capital Markets

Survey participants express ongoing concerns about the capital markets landscape, with 70% indicating that the availability of equity capital has worsened compared to a year ago, and 86% believing the availability of debt capital is also worse.

“The challenge lies less with each specific asset class and more with the broader financial markets. The ongoing Federal Reserve rate hikes, increased market illiquidity, and extensive banking regulations paint a rather uncertain picture.”

“It’s tough to raise equity for core products. Investors are interested in opportunistic strategies to deploy capital when the market bottoms out. It may be a contrarian view, but I predict there will be more money than distressed properties to buy.”

“There is capital available to borrowers who need to transact, albeit at today’s rates and returns. Those that can survive the next 36 months of resets and recalibrations will be in a good position.”

“Pension funds are allocating more dollars to credit strategies, and it is much easier to raise credit than equity capital.”

“There is plenty of equity out there, but it is far more selective, critical, and conservative than it was two years ago. The distribution of capital is highly dependent on specific sectors and asset quality. People aren’t willing to take risks and are instead sitting on their equity.”

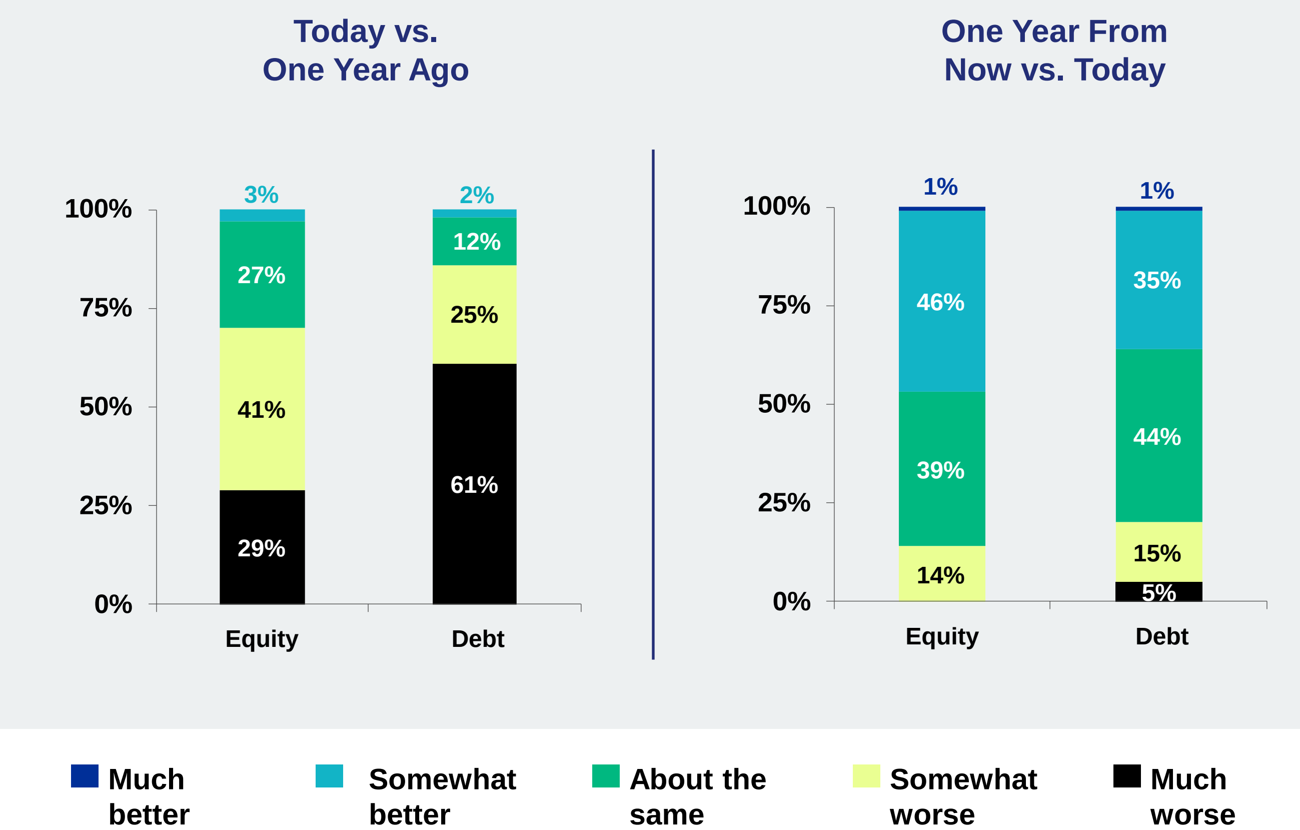
“Family offices and high net worth individuals represent untapped sources for providing equity.”

“We’re currently seeing a monumental capital raising trend for distressed funds. On top of the substantial mountain of capital already secured, there will be an additional influx of capital for distressed properties.”

Availability of Capital

% of respondents

Exhibit 4



- Regarding sentiment on the availability of equity capital, 70% believe it is worse compared to one year ago, 3% feel it has improved, and 27% believe the availability of equity remains the same
- In terms of the availability of debt capital, 86% of participants believe it is worse compared to one year ago, 2% feel it has improved, and 12% believe the availability of debt remains the same
- Looking towards the future, 47% and 36% of participants believe that equity and debt availability respectively will be better one year from now, and 14% and 20% 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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About Ferguson Partners Consulting

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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About The Real Estate Roundtable

The Real Estate Roundtable brings together leaders of the nation's top publicly-held and privately-owned real estate ownership, development, lending and management firms with leaders of major national real estate trade organizations to jointly address key national policy issues relating to real estate and its important role in the global economy.

The collective value of assets held by Roundtable members exceeds $4 trillion. The Roundtable's membership represents more than 3 million people working in real estate; 12 billion square feet of office, retail and industrial space; over 4 million apartments; and more than 5 million hotel rooms. It also includes the owners, managers, developers and financiers of senior, student, and manufactured housing—as well as medical offices, life science campuses, data centers, cell towers, and self-storage properties.

The Roundtable's policy news and more are available on The Roundtable website.

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