

# COMMERCIAL REAL ESTATE MARKET TRENDS: Q1.2017

## **Commercial Real Estate Market Trends: Q1.2017**

**Download:** [www.nar.realtor/research-and-statistics/commercial-real-estate-market-survey](http://www.nar.realtor/research-and-statistics/commercial-real-estate-market-survey)

©2017 | NATIONAL ASSOCIATION OF REALTORS®  
All Rights Reserved.

Reproduction, reprinting or retransmission in any form is prohibited without written permission. Although the information presented in this survey has been obtained from reliable sources, NAR does not guarantee its accuracy, and such information may be incomplete. This report is for information purposes only.

May 2017

## NATIONAL ASSOCIATION OF REALTORS® 2017 OFFICERS

*President*

Bill Brown

*President-Elect*

Elizabeth Mendenhall, ABR, ABRM, CIPS,  
CRB, GRI, ePRO, LCI, PMN

*First Vice President*

John Smaby

*Treasurer*

Thomas Riley, CCIM, CRB

*Immediate Past-President*

Tom Salomone

*Vice President*

Mabél Guzmán, ABR, AHWD, CIPS, CRS

*Vice President*

Kevin Sears

*Chief Executive Officer*

Dale Stinton, CAE, CPA, CMA, RCE

## CONTENTS

1   Introduction.....	5
2   Survey Highlights.....	6
3   Investment Sales .....	7
4   Leasing Fundamentals .....	10
6   Methodology.....	13



May 2017

## Introduction

Commercial space is heavily concentrated in large buildings, but large buildings are a relatively small number of the overall stock of commercial buildings. In terms of inventory, commercial real estate markets are bifurcated, with the majority of buildings being relatively small, while the bulk of commercial space is concentrated in larger buildings.

The bifurcation continues along transaction volumes as well, with deals at the higher end—\$2.5 million and above—comprising a large share of investment sales, while transactions at the lower end make up a smaller fraction.

Data are readily available for transactions in excess of \$2.5 million from several sources, including Real Capital Analytics (RCA). However, in general, data for smaller transactions—many of which are handled by REALTORS®—are less widely available. National Association of REALTORS® (NAR) *Commercial Real Estate Market Trends* gathers market information for small cap properties and transactions, mostly valued below \$2.5 million.

## Q1.2017 Update

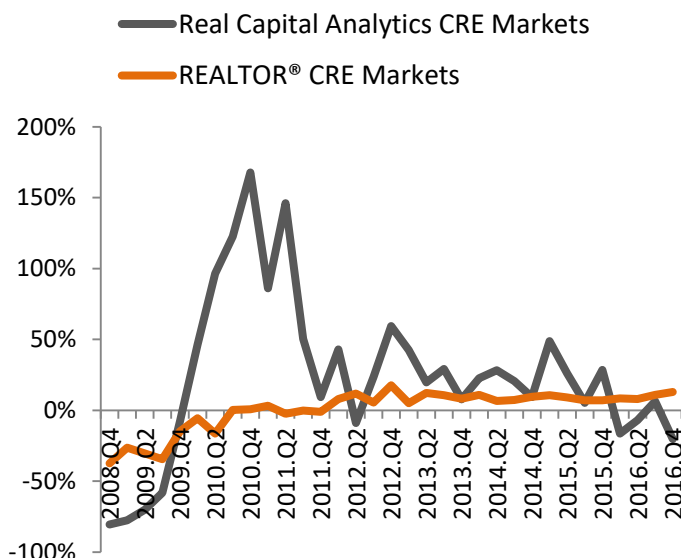
The first quarter of this year marked a change in the trend of investment sales. Sales volume in REALTORS® markets declined for the first time in five years, with a 4.4 percent slide. With tight inventory continuing to top the list of concerns, prices rose 7.2 percent from a year ago. However, cap rates began moving upward. The moves in investment metrics mirror, with a one year lag, those recorded in large cap markets, where sales volume has been declining for the past five quarters.

**GEORGE RATIU**

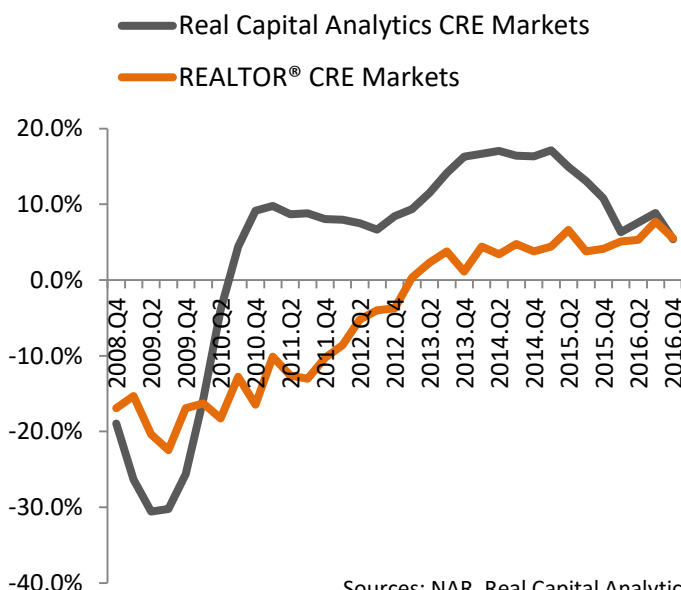
Director, Quantitative & Commercial Research

[gratiu@realtors.org](mailto:gratiu@realtors.org)

Sales Volume (YoY % Chg)



Sale Prices (YoY % Chg)



Sources: NAR, Real Capital Analytics

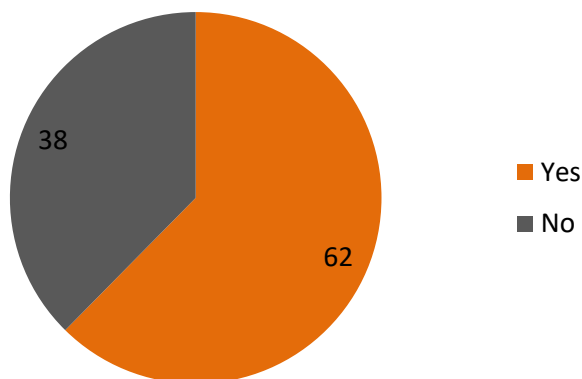
May 2017

## Survey Highlights

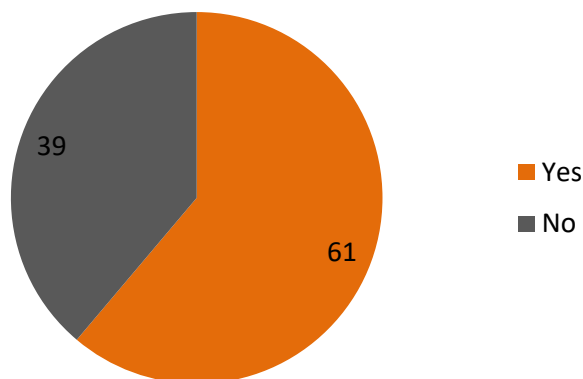
- 62.0 percent of REALTORS® closed a commercial sale.
- Sales volume declined 4.4 percent from a year ago.
- Sales prices increased 7.2 percent year-over-year.
- The average transaction value equaled \$876,500 in Q1.2017.
- 8.0 percent of REALTORS® reported an international transaction.
- The average international transaction value was \$1.0 million.

- 61.0 percent of members completed a commercial lease transaction
- Leasing volume advanced 2.3 percent from the previous quarter.
- Leasing rates increased 3.8 percent over the previous quarter.
- Concession levels declined 11.1 percent on a quarterly basis.
- Inventory shortage topped the list of current challenges, followed by buyer-seller pricing gap. Financing returned in the top three topics of concern, as small banks have been facing increased regulator scrutiny.

Sales transaction (%)



Lease transaction (%)



*Although our economy has diversified since the recession of the early 1980s, we are still heavily dependent upon pricing fluctuations in the extractive minerals industries. While the results of the recent election promises to address some of these pricing issues, until supply/demand forces return to a level that encourages new exploration, our local economy will remain more or less "inactive".*

- California

*Construction costs and building regulations are rising.*

*[Markets are] extremely bifurcated ... very strong submarkets at the same time that there are very weak submarkets in the same overall market.*

*Flagstaff market is catching up to increased demand due to population increase.*

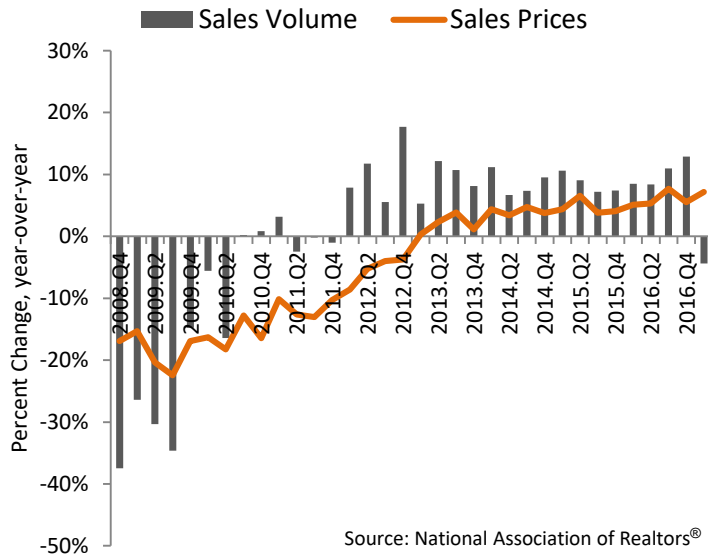
- Arizona

May 2017

## Investment Sales

The beginning of 2017 witnessed a shift in the investment landscape. Large cap markets have experienced declining sales for over a year. The first quarter of this year registered a continuation of the trend, with sales volume declining 18.0 percent.

In comparison, small cap markets posted a strong 2016, with rising sales volume. However, in the first quarter of 2017, sales volume declined 4.4 percent. In addition, a smaller percentage of REALTORS® reported closing transactions—62.0 percent in the first quarter, compared with 69.0 percent the prior quarter—a sign of slowing activity. The trend was also mirrored in a smaller average transaction value for the quarter—\$876,500 vs. \$1.1 million during the fourth quarter of 2016.



### REALTORS® Q1.2017 Prices

Office Class A (\$/SF)	\$137
Office Class BC (\$/SF)	\$91
Industrial Class A (\$/SF)	\$78
Industrial Class BC (\$/SF)	\$54
Retail Class A (\$/SF)	\$152
Retail Class BC (\$/SF)	\$104
Apartment Class A (\$/Unit)	\$59,851
Apartment Class BC (\$/Unit)	\$51,224

Source: National Association of REALTORS®

*Mid-level banking consolidation continues to reduce local lenders, whereby larger minimum loan size negatively impacts the local markets.*

*Seems foreign investors are turning towards commercial investments rather than residential.*

*I focus on working with foreign high net-worth investors (HNWI) to connect them with US sponsors forming JV on ADC projects. I like to see lenders seeking appraisers that are from the local county and familiar with the property type.*

*It is taking longer to accomplish tasks during due diligence, thus making the process cumbersome and lengthy.*

- Texas

*Lenders are looking to finance commercial real estate loans both existing and new construction. Available capital in our market/metro.*

- Virginia

*Many Sellers have unrealistic expectations on price.*

*Market is good. Rising prices and low inventory.*

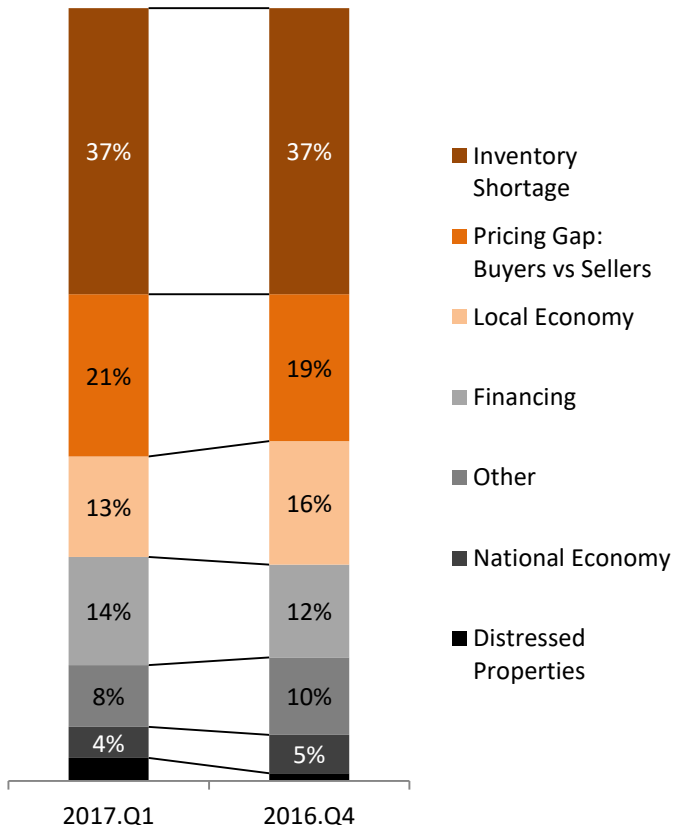
- New York

May 2017

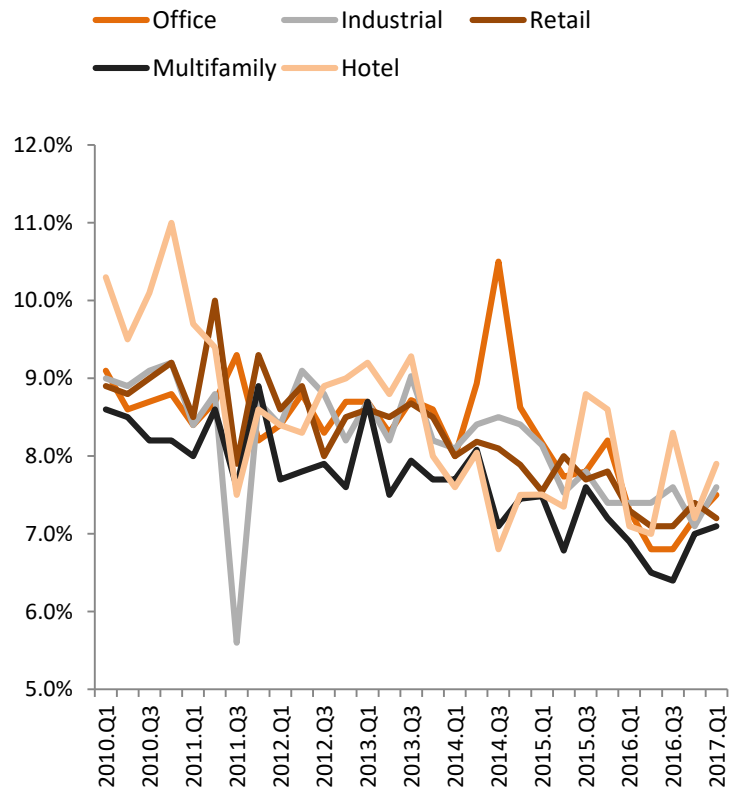
## Investment Sales - continued

The shortage of available inventory remained the number one concern for REALTORS®, and was the main driver of price movement. Prices for commercial properties increased 7.2 percent compared with the first quarter of 2016. However, capitalization rates changes indicated a likely shift in investor risk preferences. Average national cap rates reached 7.5 percent in the first quarter, 30 basis points higher than the same period in 2016. The rate on first-quarter 10-year Treasury Notes averaged 2.2 percent, maintaining a wide spread to cap rates in REALTOR® markets.

### REALTORS® Most Pressing Challenges



### REALTORS® Commercial Capitalization Rates



Source: National Association of Realtors®

### REALTORS® Q1.2017 Cap Rates

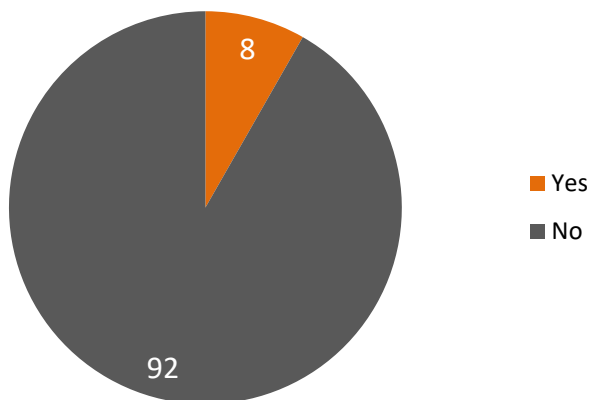
Office Class A	7.0
Office Class BC	8.0
Industrial Class A	7.1
Industrial Class BC	8.1
Retail Class A	6.6
Retail Class BC	7.9
Apartment Class A	6.4
Apartment Class BC	7.8
Hotel Class A	7.1
Hotel Class BC	8.6

Source: National Association of REALTORS®



May 2017

Members with International Transaction (%)

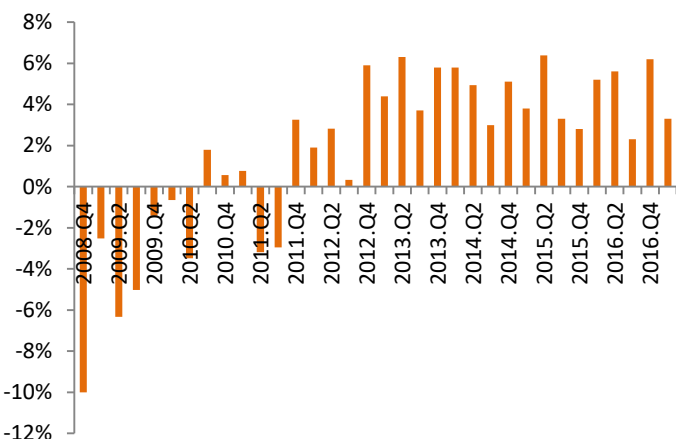


## Investment Sales - continued

International transactions remained a noticeable share of REALTORS®' activity, comprising 8.0 percent of responses. The average international sale price was \$1.0 million in the fourth quarter of this year. The average cap rate for international deals was 6.7 percent.

Respondents indicated that the direction of commercial business opportunities during the first quarter of 2017 rose at a slower pace than the prior quarter: 3.3 percent compared with 6.2 percent in the fourth quarter of 2016, and 5.2 percent a year ago. Financing returned as a top concern in REALTORS®' markets, with 14.0 percent of members finding inadequate funding for commercial transactions.

Direction of Business Opportunity (QoQ)



Source: National Association of Realtors®

*The market is getting better but the rates are still down, and tenants are still very cautious. Seems to be a good many buyers out there, but they want high cap rates - so there is a big gap between buyers and sellers, and properties for sale are scarce.*

- Utah

*Very active... seller's market, but there is only so much an investor is willing to pay for an investment property in Columbus, Ohio. There is a difference between the private investor and the corporate investors. The large corporate deals sell for a lower cap rate to a national buyer. In the mid-range deals, the buyers are more conservative about cap rates, location, and condition.*

- Ohio

*The market is in bad shape [due to] regulations; competition is saturated, mostly cash buyers and investors, very few families getting approved for loans due to student loan debt and because most are running their own small businesses. [...] Rental market has dried up with low qualifying renters. Places like Pasadena and South East Texas have extremely overpriced homes, where places like Palestine and Rural East Texas are underpriced.*

- Texas

May 2017

## Leasing Fundamentals

Commercial fundamentals remained positive in the first quarter of 2017. However the pace of growth moderated. Leasing volume advanced by 2.3 percent from the preceding quarter. New construction increased by 2.3 percent from the prior quarter, the slowest pace since the first quarter of 2015. Leasing rates rose by 3.8 percent, as concessions declined 11.1 percent.

*For industrial, low vacancy rate, not a lot of inventory available or in the pipeline, rental rates have been increasing....seller's/landlord's market.*

*I lease office suites for the owner of the building my office is located in, and I am also the property manager. There is a great need for office space for small businesses that does not break the bank.*

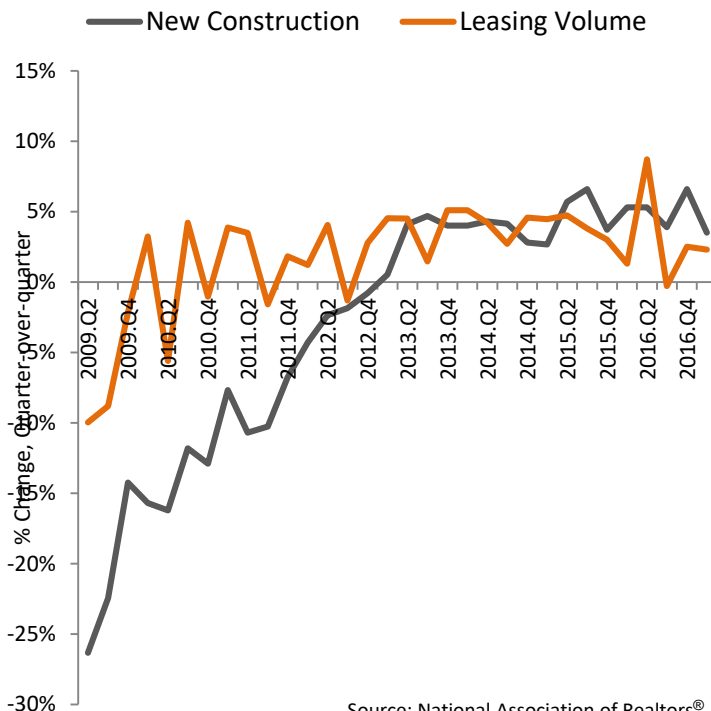
*Increase in activity; decrease in inventory. Developers cannot build due to disparity in building costs versus potential income stream*

*[There are a] lot of failures of small franchises and brick and mortar retailers. Online shopping seems to be a factor*

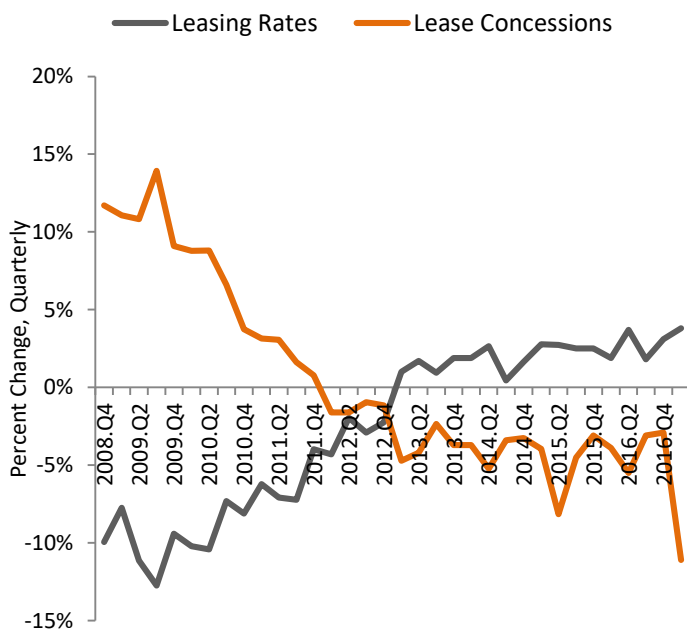
*Market remains strong with some apartment overbuilding starting to show up.*

*Outside of the urban core and a few hot markets, much of the farther out suburbs are still marginal and overbuilt.*

*The current commercial market is good. We are experiencing some big box retail closures in key centers, [which] cause the owner to find a new tenant, or create a different center.*



## REALTOR® Commercial Leasing Trends



May 2017

## Leasing Fundamentals - continued

Tenant demand remained strongest in the 5,000 square feet and below segment, accounting for 84.0 percent of responses. Demand for space in the “Under 2,500 square feet” segment was virtually unchanged from the last quarter, capturing 45.0 percent of responses. Demand for properties in the “10,000 - 49,999 square feet” segment notched a noticeable jump, accounting for 11.0 percent of total responses, an almost two-fold increase from the prior quarter.

*Finding quality commercial appraisers to add to my firm is a difficult task. Training maybe the only long-term option.*

*While we have some modest increase in construction, we have not yet seen overall activity match the general optimism that keeps being reported on the news here locally.*

*People feel trust to move forward with business plans now - just need stifling regulations removed*

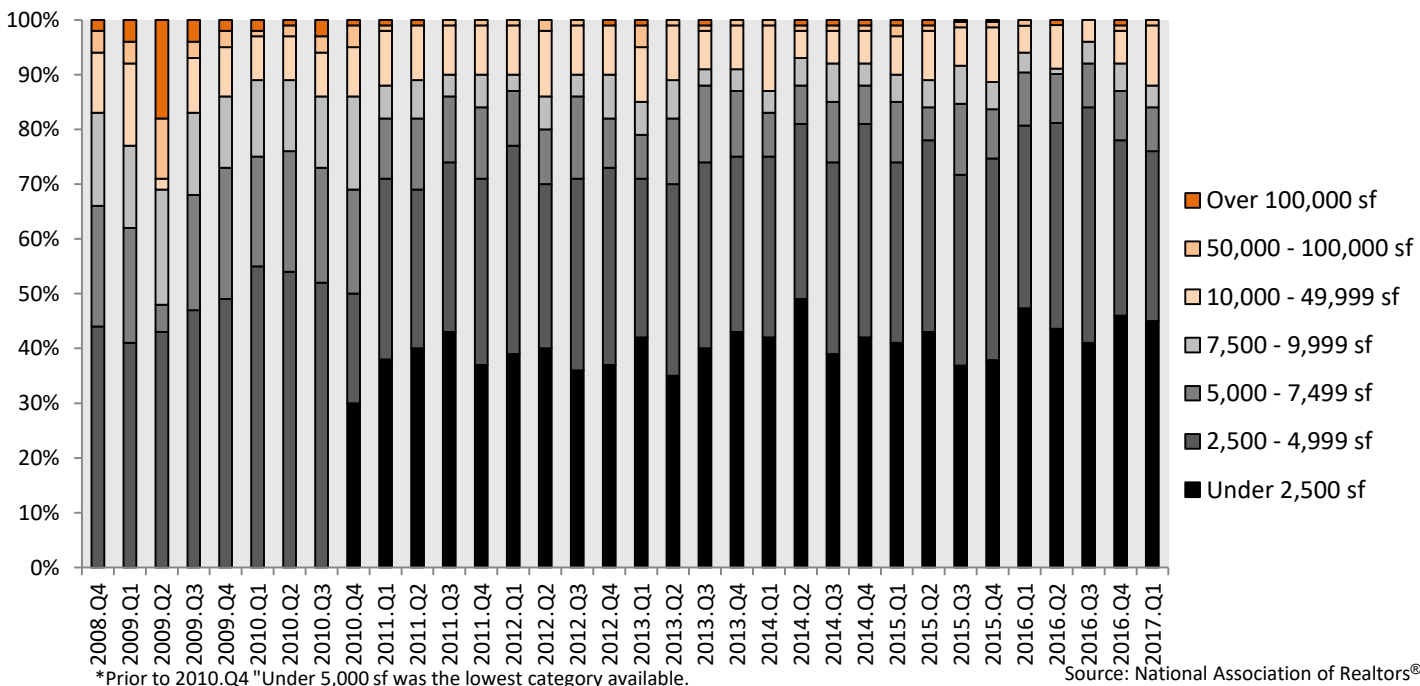
*The overall San Antonio market continues to be strong will low unemployment and new companies locating to the area. Hulu just announced a 500-person office to be located in San Antonio.*

- Texas

*There is limited commercial activity in smaller towns like this area. I travel outward about 150 miles from my hometown to stay busy with agricultural and general commercial appraisals.*

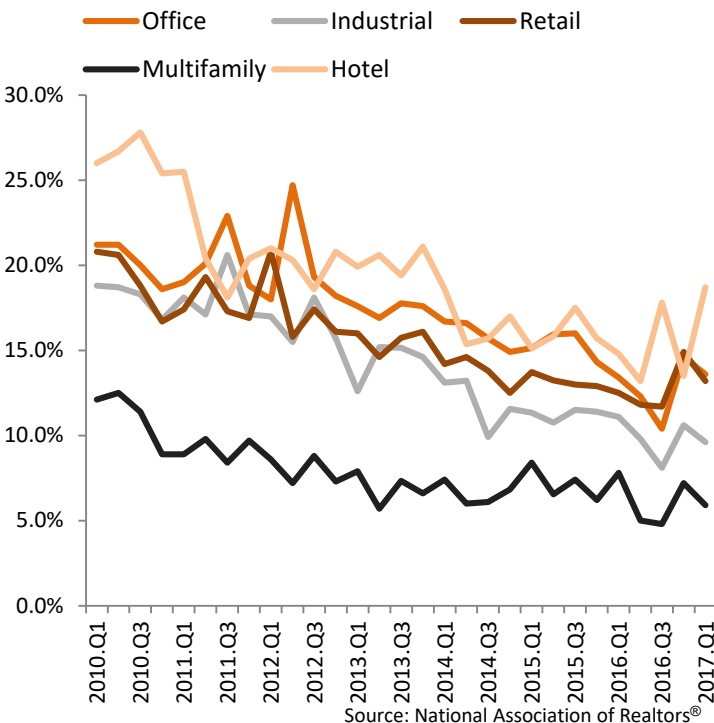
*We are a stable market with low operating costs and a good, available skilled labor pool.*

Average Leased Space by Size, Quarterly\*



May 2017

## REALTORS® Commercial Vacancy Rates



## Leasing Fundamentals - continued

Vacancy rates continued declining in the first quarter of this year. Lease terms remained steady, with 36-month and 60-month leases capturing 61.0 percent of the market. One-year and two-year leases made up 23.0 percent of total.

During the quarter, 61.0 percent of REALTORS® reported closing a lease transaction. NAR members' average gross lease volume for the quarter was \$654,000.

### REALTORS® Q1.2017 Vacancy Rates

Office	13.6	%
Industrial	9.6	%
Retail	13.2	%
Multifamily	5.9	%
Hotel	18.7	%

### REALTORS® Q1.2017 Rents

Office	\$46 / Sq.Ft.
Industrial	\$31 / Sq.Ft.
Retail	\$55 / Sq.Ft.
Multifamily	\$747 / Unit

## Q1.2017 Market Opportunities

Apartments Location Local Economy Town Land  
 Expansion Inventory Highway Properties  
 New Construction Growth Projects  
 Development Finding Industrial  
 Multi Family Market Force Low Competition  
 Space Place Demand Increases Prices Tearing  
 Retail Cash

May 2017

## Methodology

The REALTORS® Commercial Real Estate Market Trends measures quarterly activity in the commercial real estate markets, as reported in a national survey. The survey collects data from REALTORS® engaged in commercial real estate transactions. The survey is designed to provide an overview of market performance, sales and leasing transactions, along with information on current economic challenges and future expectations.

In April 2017, NAR invited a random sample of 62,212 REALTORS® with an interest in commercial real estate to complete an on-line survey. A total of 799 complete responses were received, for an overall response rate of 1.3 percent. The main measure of central tendency employed in the analysis is the mean.







The National Association of REALTORS®, “The Voice for Real Estate,” is America’s largest trade association, representing 1.2 million members, including NAR’s institutes, societies and councils, involved in all aspects of the real estate industry. NAR membership includes brokers, salespeople, property managers, appraisers, counselors and others engaged in both residential and commercial real estate. The term REALTOR® is a registered collective membership mark that identifies a real estate professional who is a member of the National Association of REALTORS® and subscribes to its strict Code of Ethics. Working for America’s property owners, the National Association provides a facility for professional development, research and exchange of information among its members and to the public and government for the purpose of preserving the free enterprise system and the right to own real property.

## **NATIONAL ASSOCIATION OF REALTORS® RESEARCH DIVISION**

The Mission of the National Association of REALTORS® Research Division is to collect and disseminate timely, accurate and comprehensive real estate data and to conduct economic analysis in order to inform and engage members, consumers, and policy makers and the media in a professional and accessible manner.

To find out about other products from NAR’s Research Division, visit [www.nar.realtor/research-and-statistics](http://www.nar.realtor/research-and-statistics)

**NATIONAL ASSOCIATION OF REALTORS®  
RESEARCH DIVISION**  
500 New Jersey Avenue, NW  
Washington, DC 20001  
202.383.1000

# COMMERCIAL REAL ESTATE MARKET TRENDS: Q1.2017