Q2 2024

Commercial Real Estate Industry Conditions & Sentiment Survey

US results and analysis

Introduction

Q2 2024
Commercial Real Estate Industry Conditions & Sentiment Survey

Altus Group is pleased to share the results of our Commercial Real Estate Industry Conditions & Sentiment Survey for the US with survey participants and partners. This survey was conducted by Altus Group's Research Team in an effort to provide insights into the market sentiment, conditions, metrics, and issues affecting the commercial real estate (CRE) industry.

The survey captures the individual practitioner's perspective, representing various functions and across the capital stack. Participation in the survey is voluntary and responses will remain confidential.

As always, we invite you to share any feedback or questions with your Altus Group contact or reach out to Altus Group's Research Team directly at altusresearch@altusgroup.com.

Omar Eltorai
Director of Research, Altus Group's Research Team

Cole Perry
Senior Market Analyst, Altus Group's Research Team

CRE Industry Conditions & Sentiment Survey Q2 2024 - US

Methodology

Survey size and methodology

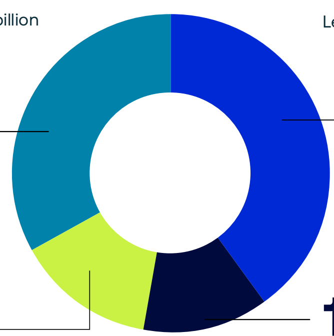
Altus Group's Research Team surveyed industry participants across the US from March 25 to April 29, 2024. There were 227 respondents, representing at least 49 different firms[1].

Questions in the survey were optional and explored two main topics: current conditions and future expectations. Percentages represent the share of all responses received for each question, excluding "blank" or "not applicable" responses.

227 responses

49 different firms[1]

Firm CRE exposure ($USD)



[1] Firm count based on participants who chose to identify themselves.

Functional area

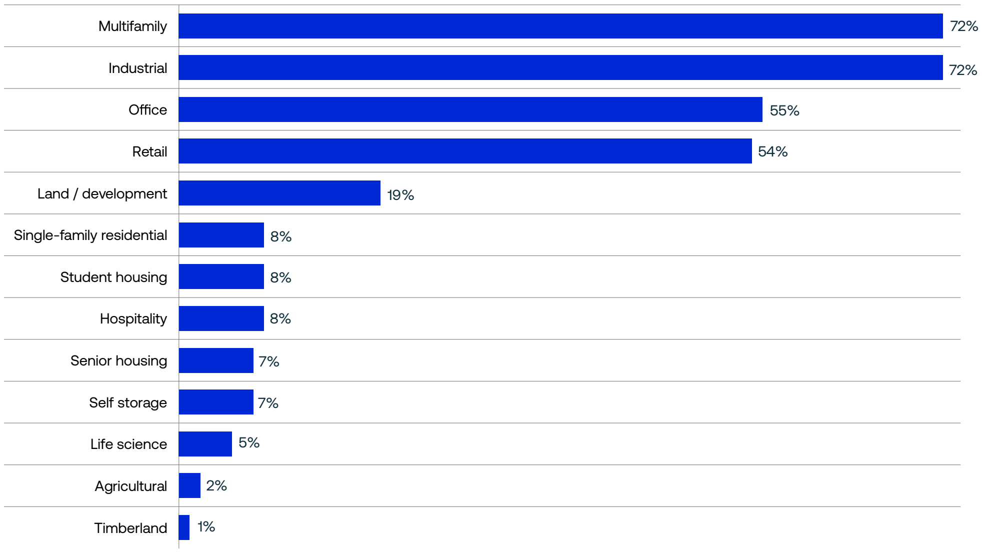
Appraiser / valuations	23%
Senior management / executive leadership	17%
Brokerage (investment sales or leasing) Fund	11%
Fund or portfolio manager	10%
Acquisitions / dispositions	7%
Investment strategy / investment research	6%
Asset manager / FP&A	4%
Corporate (HR, IT, legal, marketing, accounting)	4%
Debt capital markets / mortgage banker	4%
Equity investor	3%
Investor relations / fundraising	2%
Loan officer / credit risk manager	2%
Originations / underwriting	2%
Equity capital markets	1%
Property management	1%
Developer / construction manager	1%
Other	1%

Organization type

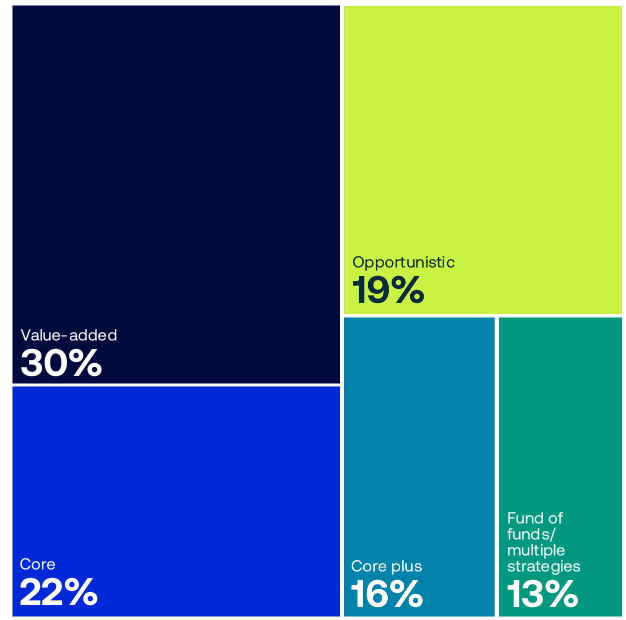
Advisory	21%
Brokerage	16%
Investment manager	13%
Private equity	11%
Service provider	10%
Asset management company	8%
Developer	5%
Bank	4%
Equity REIT	2%
Pension Fund	2%
Family office or sovereign wealth fund	1%
Non-bank lender	1%
Endowment or foundation	1%
Insurance company	1%
Other	1%

Respondent characteristics

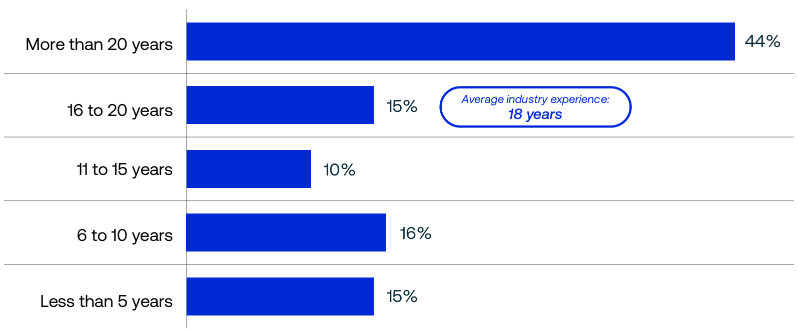
What property types does your firm primarily focus on?



How would you describe your firm's primary investment strategy?



How many years of experience do you have in the industry?



Note: Percentages represent the share of all responses, excluding "blank" or "not applicable" responses.

CRE Industry Conditions & Sentiment Survey Q2 2024 - US

Conditions

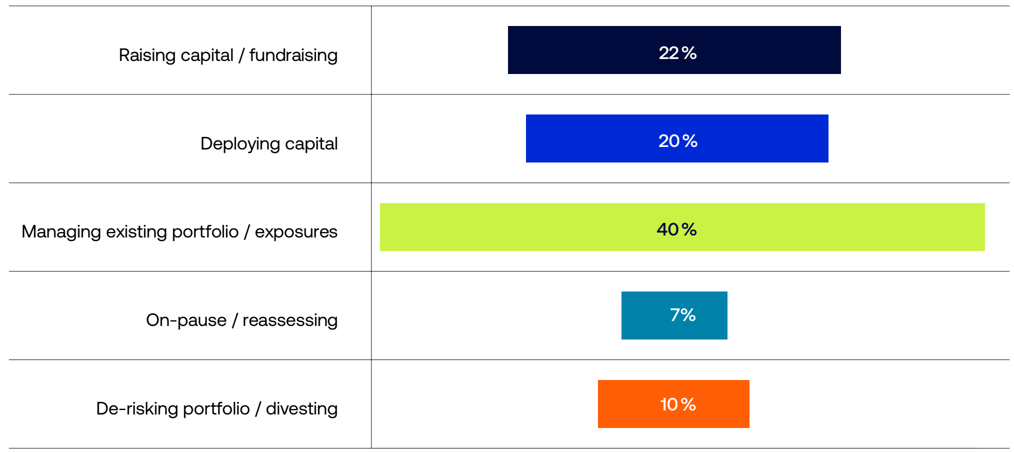
Current focus

Near-term de-risking picks up slightly as a primary focus. A greater portion of participants reported being focused on capital derisking/ divesting, with responses up six percentage points to 10%. The share of US respondents reporting "deploying capital" as their primary focus over the next six months declined slightly from 25% in Q1 2024 to 20% in Q2 2024. The share of respondents focused on raising capital or managing their existing portfolios remained nearly flat quarter-over-quarter in Q2 2024 at 40%.

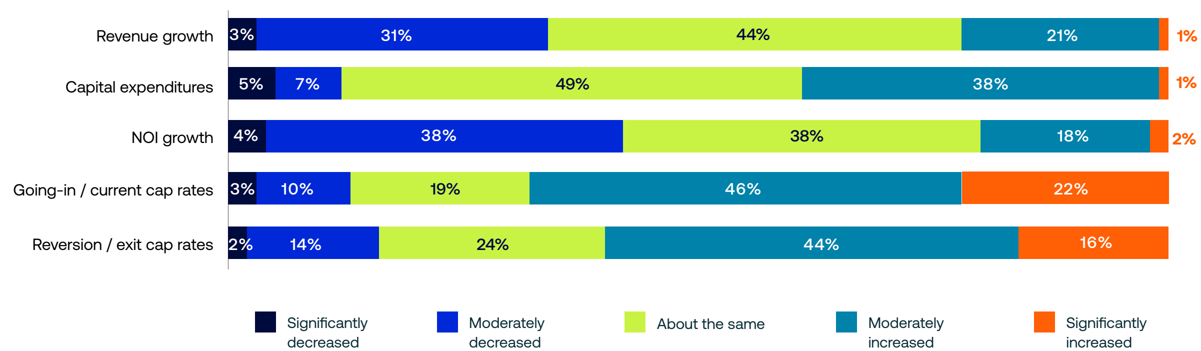
Broad majorities note increased expectations for cap rates; capital expenditure assumptions stabilizing. More than one in three respondents noted increased expectations for revenue growth while a plurality (42%) noted increased expectations for NOI growth. More than 20% of respondents stated that their expectations for revenue and NOI growth had either moderately or significantly increased while the fraction of respondents stating that expectations for both were "about the same" remained relatively stable quarter-over-quarter, suggesting that cash-flow expectations continue to stabilize.

Expectations for capital expenditures have somewhat stabilized as well, with nearly half of respondents indicating that their expectations for capital expenditures remained "about the same" relative to 12 months ago, though nearly four in ten state that their expectations have increased. A broad majority of respondents noted moderate to significant increases in their expectations for going-in and current cap rates, with 16% and 22% stating expectations for going-in / current cap rates and reversion / exit cap rates have significantly increased.

What do you think your team's primary focus will be over the next 6 months?



How have your expectations for your portfolio changed compared to 12 months ago?

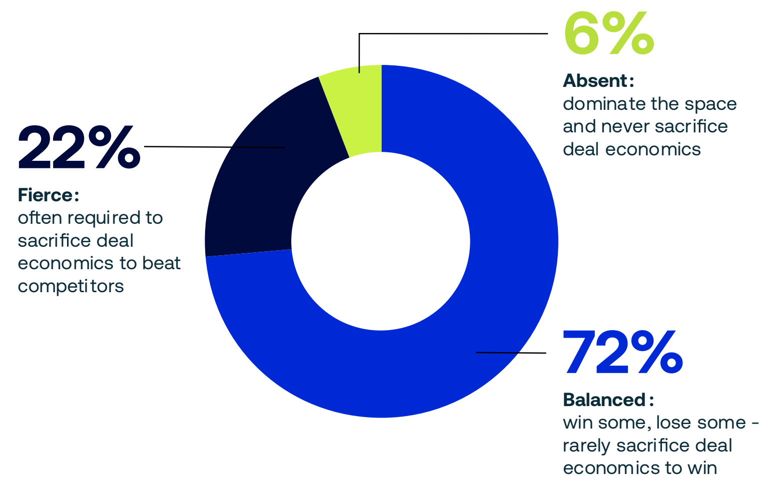


Note: Percentages represent the share of all responses, excluding "blank" or "not applicable" responses.

Competition and pricing

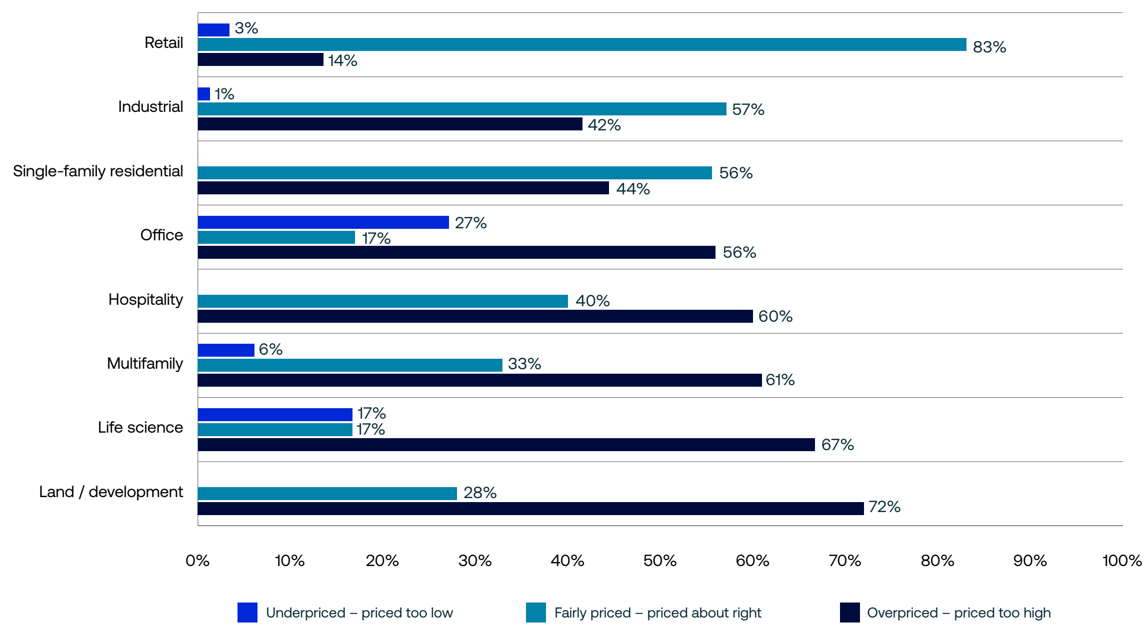
Competition is steady versus the prior two quarters as properties approach "fairly priced". Similar to the previous two quarters, while just over one in five (22%) described current market competition as "fierce: often required to sacrifice deal economics to beat competitors", a wide majority (72%) of respondents described the current level of competition as "balanced: win some, lose some". Across the four main property sectors (industrial, multifamily, office, retail), the characterization of "fairly priced" increased by eight percentage points (pp) compared to Q1 2024 results – despite more than half of respondents characterizing multifamily (61%) and office (56%) as "overpriced". However, the highest levels of reported "overpricing" were found in the smaller sectors, most notably land / development (72%) and life science (67%).

How would you describe the level of competition among your firm's peer group?



Compared to the prior quarter, the largest shift in perceived priciness was seen in the hospitality sector, which saw a 40 pp increase in reported "overpriced" characterization from Q1 2024, when it was viewed as "fairly priced" by the majority of respondents. Another notable shift was seen in retail, which saw a 12 pp increase in the "fairly priced" characterization and a 2 pp increase in the "overpriced" characterization, as 14 pp fewer respondents characterized it as "underpriced" when compared to the prior quarter. Finally, office saw a 7 pp shift over the quarter to the "underpriced" characterization; indicating that nearly half (44%) of respondents view the sector as being either "underpriced" (27%) or "fairly priced" (17%).

How would you characterize current pricing for the following property types?

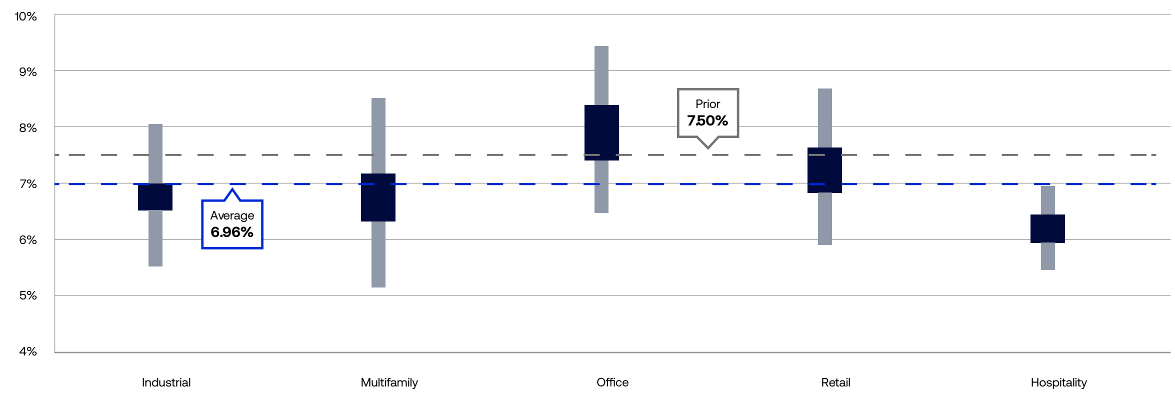


Note: Percentages represent the share of all responses, excluding "blank" or "not applicable" responses.

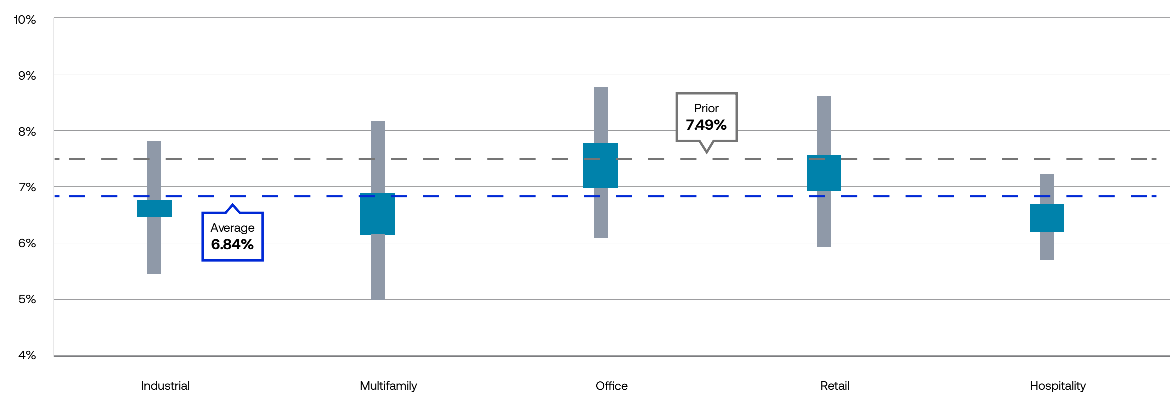
What all-in interest rates are you seeing in the market?

Debt financing costs drop across term, rate type, and collateral; most for hospitality and least for retail. The reported cost of debt financing seen in the market improved on the quarter, across different loan terms, rate types (fixed or floating), and collateral property types. The average all-in debt financing cost seen in the current market by survey respondents dropped by 57 bps and 69 bps on average for 5-year and 10-year debt structures, respectively. However, much of this was driven by hospitality, which saw reported debt costs come down by more than 200 bps on the three debt structures. Retail was the property type that experienced the least amount of change compared to the prior quarter – as the reported all-in interest rate on 5-year floating rate structure increased 5 bps and 3 bps for the 10-year fixed rate while declining by only 2 bps for the 5-year fixed rate structure.

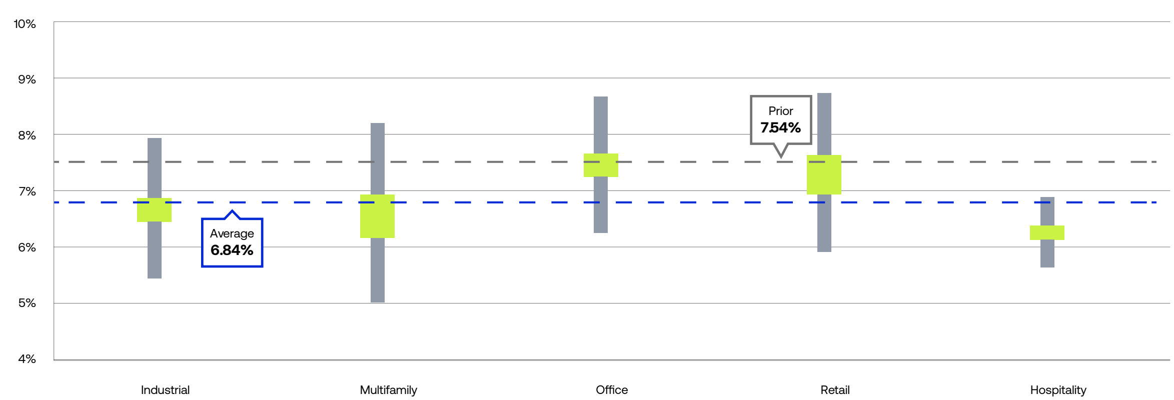
5-Year Floating Rate (%)



5-Year Fixed Rate (%)

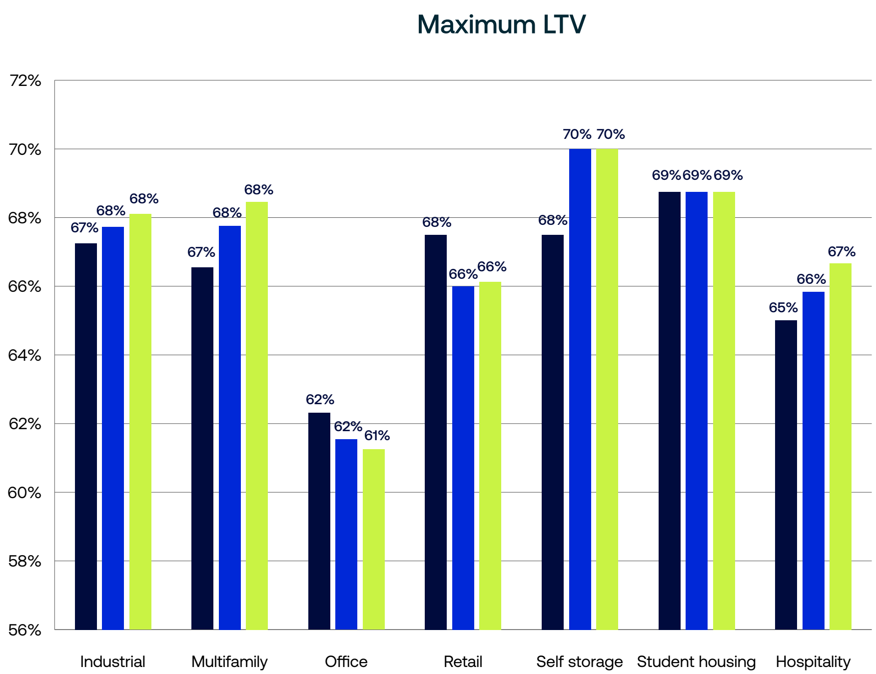


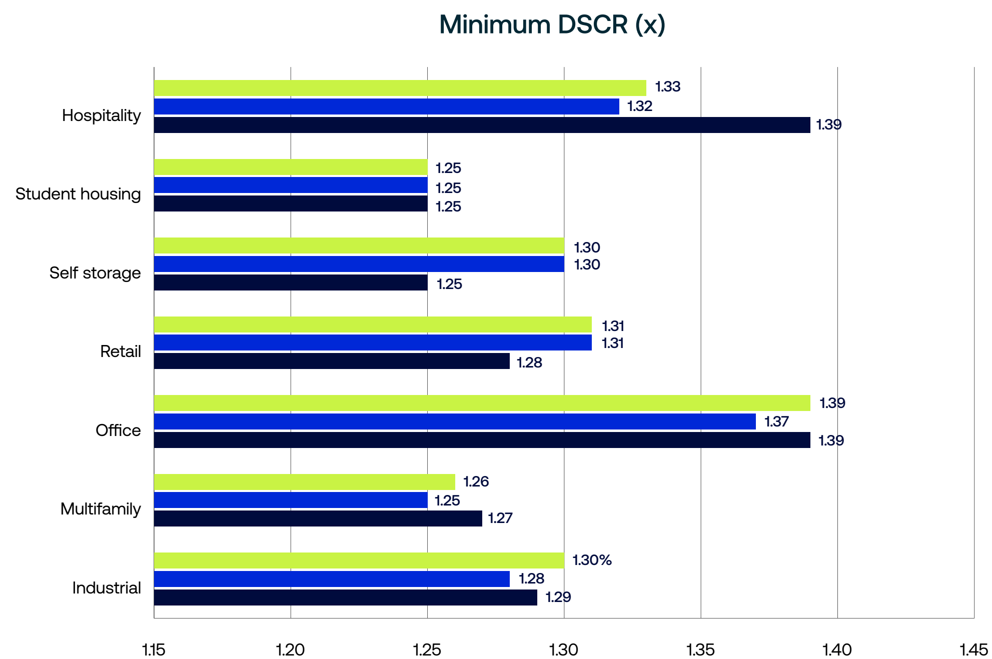
10-Year Fixed Rate (%)



What senior debt financing terms are you seeing in the market?

Leverage increases slightly on the quarter, as lenders loosen. Respondents in Q2 2024 noted maximum loan-to-value (LTV) ratios increased by 4 pp and debt service coverage ratios (DSCR) decreased by 1 basis point (bps) on average across the four main property types compared to the prior quarter. The most notable LTV increases were in office (6 pp) and industrial (4 pp). Across the different loan types, the 10-year fixed rate structure had the largest increase in LTV on average, while the 5-year fixed rate structure had the largest decrease in minimum DSCR when compared to the prior quarter.



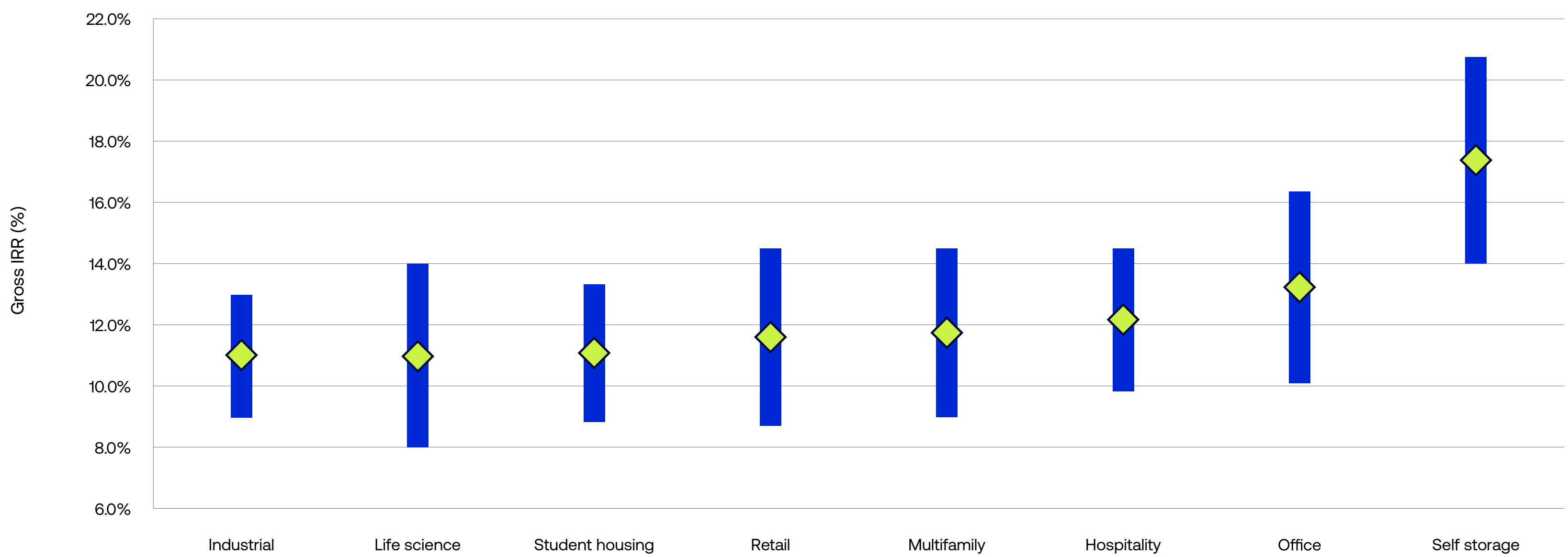


5Y Floating 5Y Fixed 10Y Fixed

Reported current market gross IRRs

New fund-targeted gross IRRs increase modestly across property sectors over the prior quarter. Targeted gross IRRs seen marketed for new funds and deals averaged 12.4% across all property types in Q2 2024, up 60 bps from the prior quarter. Across the four main property types (retail, multifamily, office, industrial), the reported average gross IRR was 12.2%, up 130 bps from Q1 2024. The largest quarterly increases in reported gross IRR midpoints were seen for self-storage and office, which increased by 571 bps and 121 bps, respectively to 17.4% and 13.2% in Q2 2024. The largest midpoint IRR quarterly declines were reported for life science and hospitality, which saw decreases of 410 bps and 83 bps, respectively, over the prior quarter to 11.0% and 12.2%.

What are typical ranges for the returns you are seeing across the current market for new funds?

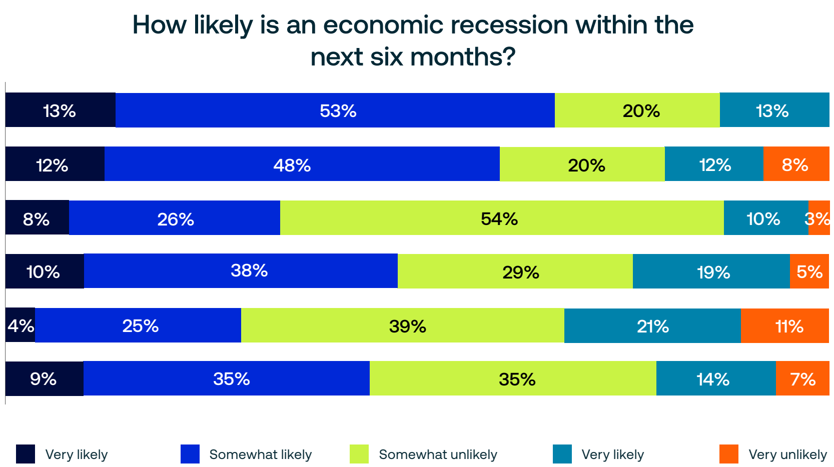


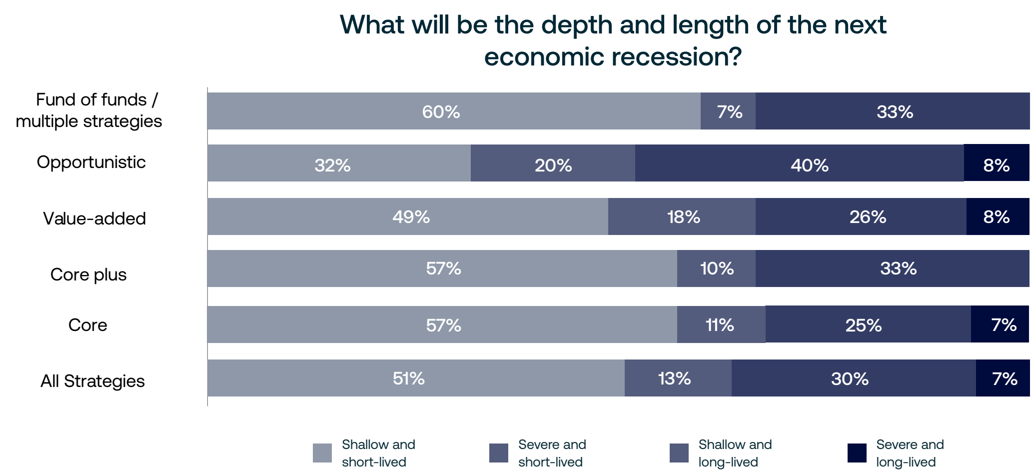
CRE Industry Conditions & Sentiment Survey Q2 2024 - US

Sentiment & expectations

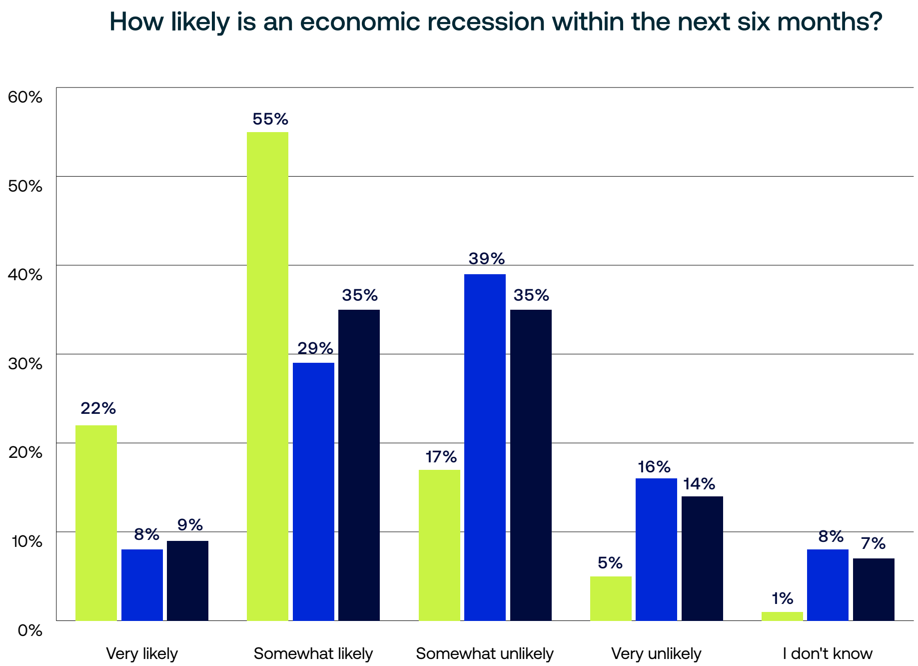
Recession expectations

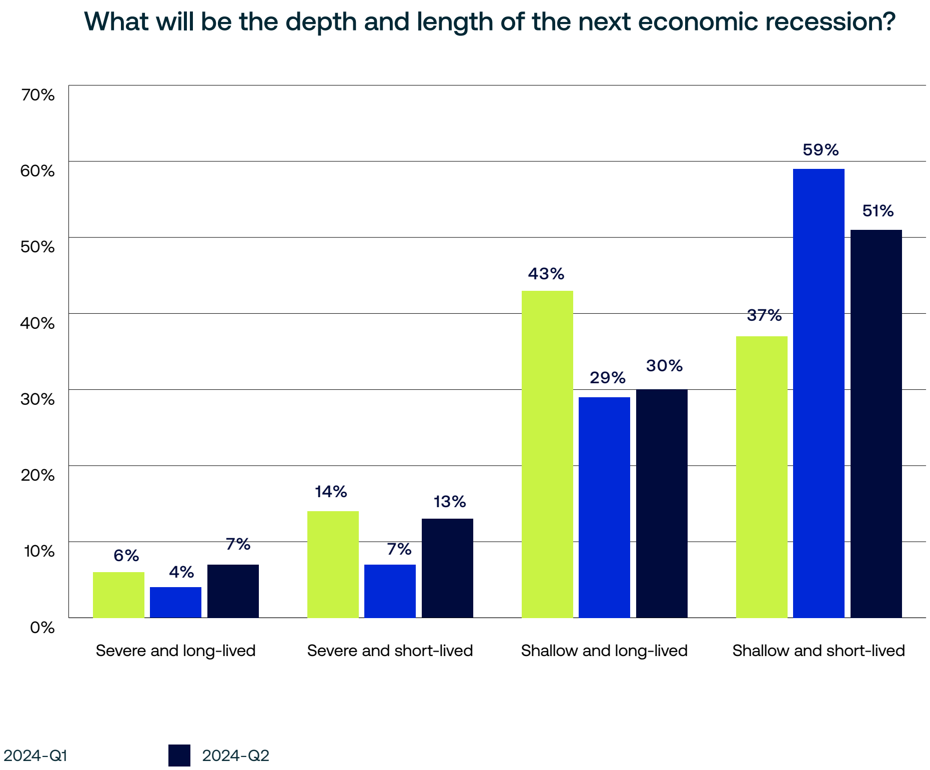
Recession concerns tick up slightly and the anticipated magnitude worsens. While the majority (49%) of respondents do not anticipate a near-term recession, those saying that a recession in the next 6 months is likely ("very likely" and "somewhat likely") increased by 7 pp from the prior quarter. This shift means that the majority of the industry (70%) currently sits in the "somewhat" camp – responding either "somewhat likely" or "somewhat unlikely". Across the different strategies, respondents who identified as having a core strategy remain the least expectant of a near-term recession, and those with fund of funds and opportunistic strategies are the most expectant. However, fund of funds, opportunistic, and core strategies all saw quarterly increases in respondents who anticipate a near-term recession. And while the overall portion of respondents who said "I don't know" remained small (7%, down 1 pp from Q1 2024), both core and core plus strategies saw quarter-on-quarter increases. While the majority (80%) of respondents expect the next recession to be shallow (either "shallow and short-lived" or "shallow and long-lived"), this was down from the prior quarter (89%), as those who responded that they expect the next recession to be "severe" (either "severe and short-lived" or "severe and long-lived") increased by 9 pp across all strategies and by 11 pp in core and 10 pp in opportunistic strategies.





Recession expectations



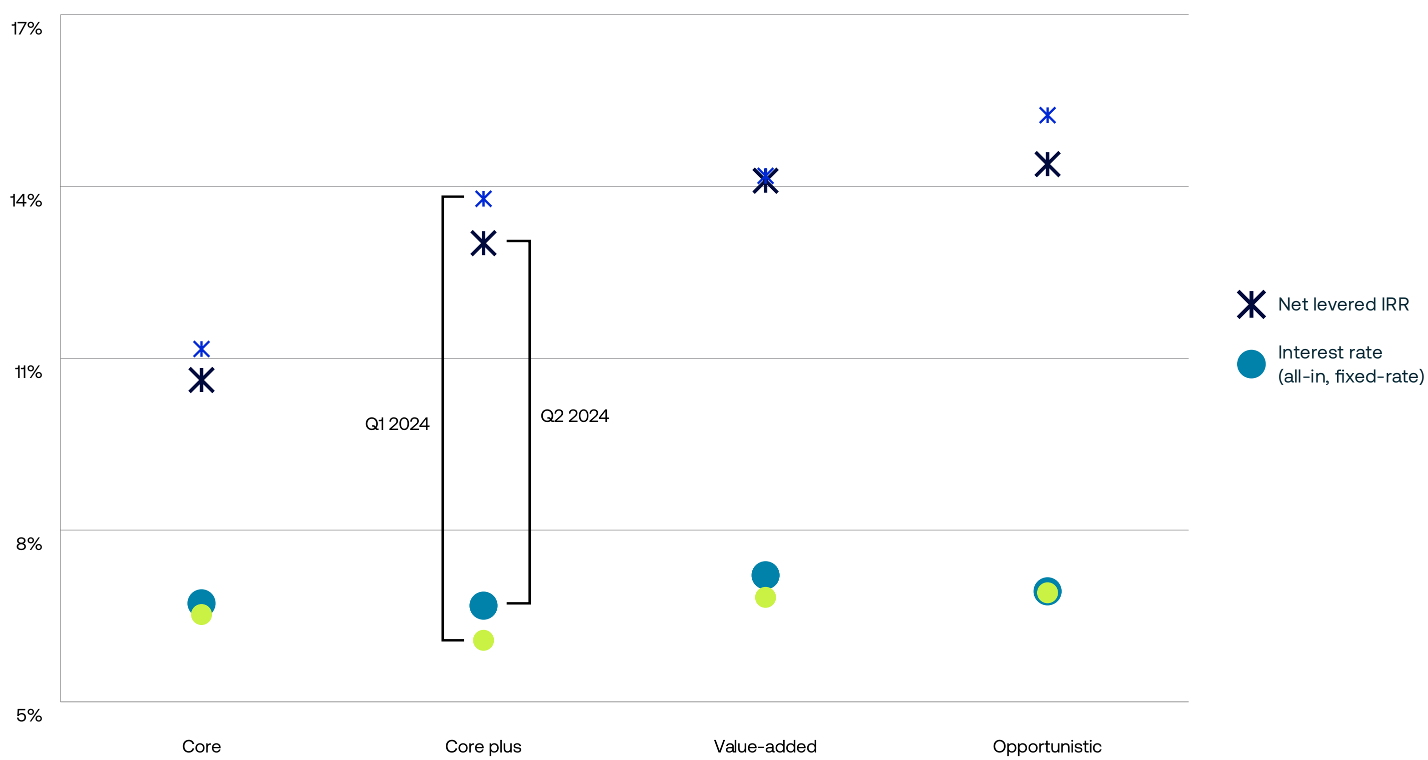


Cost of capital expectations

Expected returns to equity moderate slightly as anticipated cost of debt increases. Respondents' 12-month forward view of all-in, fixed-rate financing increased moderately to a range of 6.7-7.3% across the main equity portfolio strategies, compared to the 6.1-6.9% range reported in the prior quarter. Expectations of the cost of debt over the next year increased by an average of 35 bps across all strategies over the prior quarter.

The increase in debt costs was accompanied by a decrease in net returns to equity (net levered IRRs), which across all strategies decreased by 51 bps on average compared to the prior quarter. The biggest shifts were seen in the core plus and opportunistic strategies, where anticipated net IRRs were 73 bps and 81 bps on the quarter, respectively.

Where do you anticipate the cost of capital to be over the next 12 months (on annualized basis)?



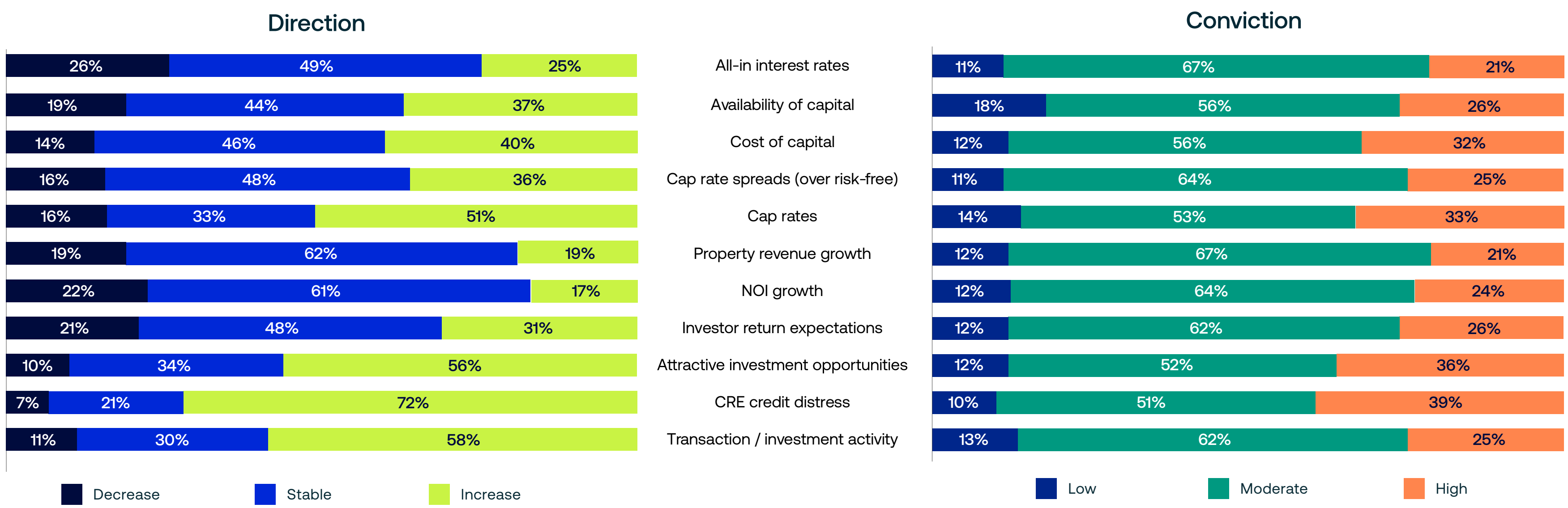
What changes do you anticipate to the following key metrics over the next 12 months?

Capital environment is expected to remain challenging. The majority of respondents indicated that in aggregate they expect interest rates to remain stable (49%) over the next 12 months – while the portion of those expecting an increase (25%) was up 16 pp compared to the prior quarter and those expecting interest rate decreases (26%) fell by 20 pp. More than a third (37%) of respondents expect increased availability of capital in the next year, up 9 pp from last quarter. Two-fifths (40%) of respondents expect the cost of capital to increase in the next 12 months up 12 pp from Q1 2024.

Higher conviction for higher cap rates. Similar to last quarter, approximately one-sixth of respondents (16%) expect cap rates to decrease over the next 12 months, while the majority (51%) expect cap rates to increase, a 13 pp increase from the prior quarter. While the expectations for cap rate spreads were less changed on the quarter, and the majority (48%) of respondents still expect cap rates spreads to be stable, the conviction for both cap rates and cap rate spreads increased by 9 pp and 10 pp over the quarter.

Revenue and NOI growth expectations improve. Participants generally still expect revenue growth to be stable (62%) over the next 12 months, though 19% expect revenue growth to increase, up 2 pp from the prior quarter. Participants expect NOI growth to be stable (61%) or decrease (21%). Compared to the prior quarter, these results increased by 8 percentage points and fell by 13 percentage points, respectively. Revenue and NOI growth expectations taken together could suggest that owners are anticipating a more stable cash flow environment ahead.

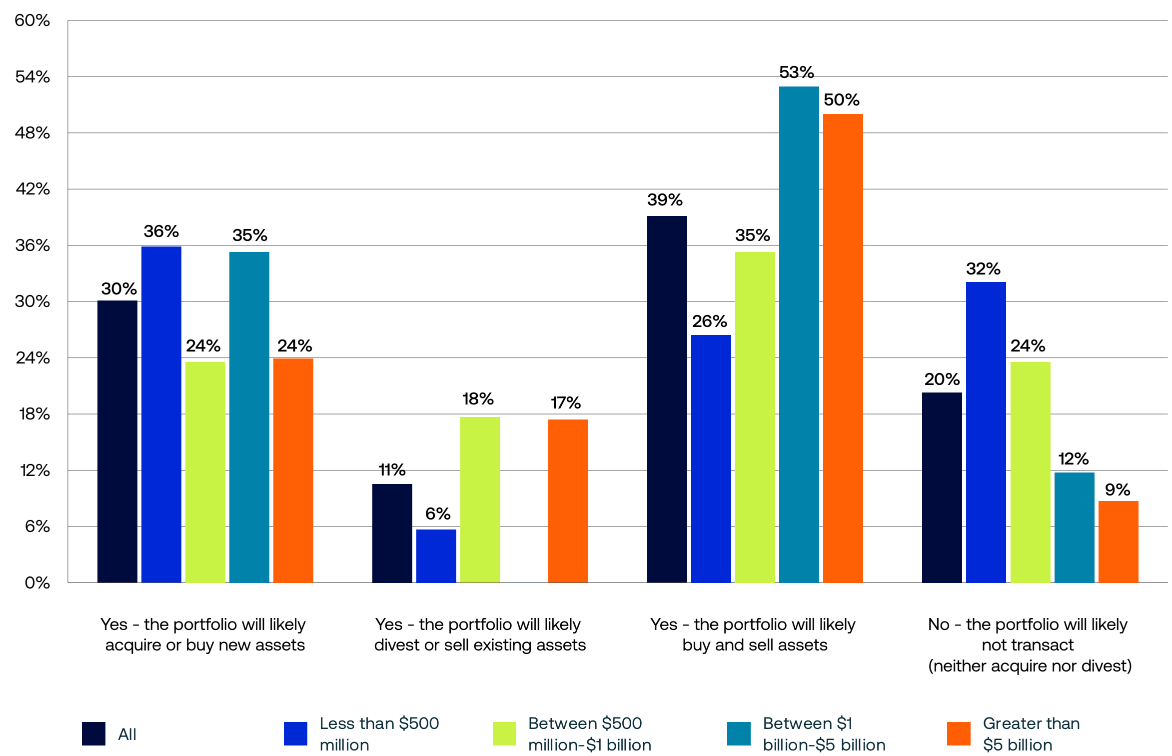
Slightly more conviction around slightly less distress. 72% of respondents expect CRE distress to increase over the next 12 months, down 4 percentage points from the prior quarter, with 39% of participants noting high conviction in their directional call – a 10 pp increase from Q1 2024. Despite an expected increase in distress, over half of the participants expect attractive investment opportunities and transaction activity to increase (56% and 58%, respectively) over the next year.

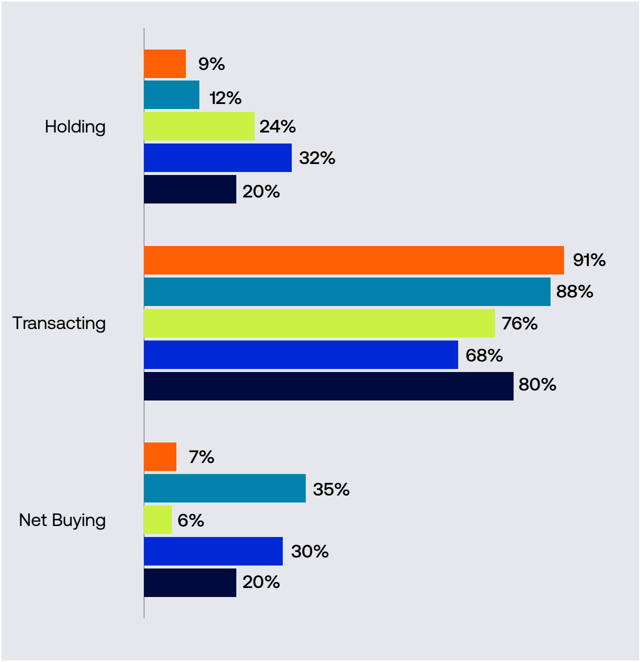


Transaction intentions over next 6 months

Smaller firms signal intent to sell, while largest firms show more transaction appetite. Respondents indicated that they anticipate market activity to pick up over the coming 6 months, with the majority (80%) of survey participants anticipating transacting (buying, selling, or both) to be the same as the prior quarter. While 91% of the largest firms (greater than $5 billion) signaled intent to transact (buy, sell, or both) in the near term, up from 83% in Q1 2024, smaller firms (CRE exposure between $500 million -$1 billion) saw a 33 pp decline in buying intention, 18 pp increase in selling intention and 17 pp increase in intention to hold.

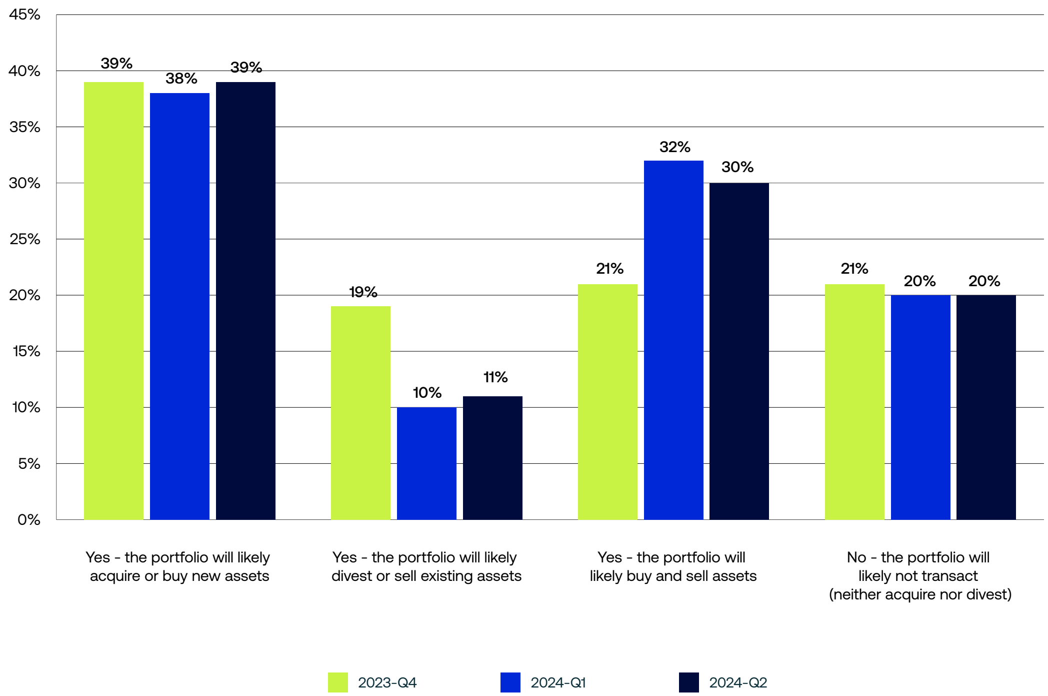
Over the next 6 months, do you anticipate any transactions in your portfolio?

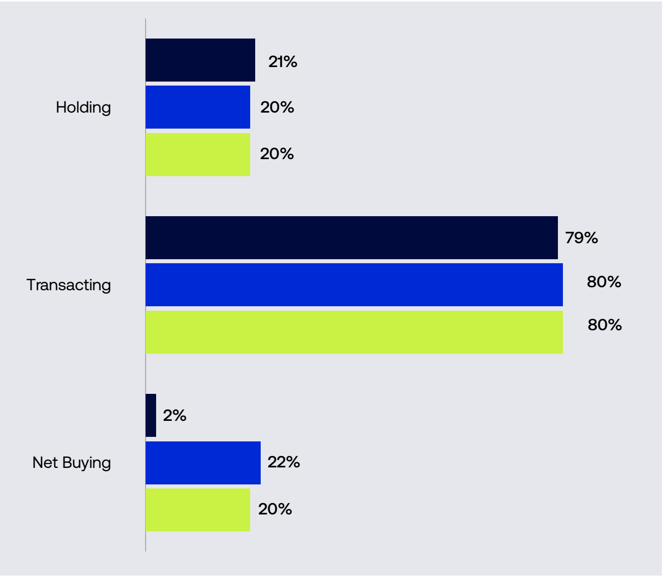




Transaction intentions over next 6 months

Over the next 6 months, do you anticipate any transactions in your portfolio? (Quarter-over-quarter comparison)

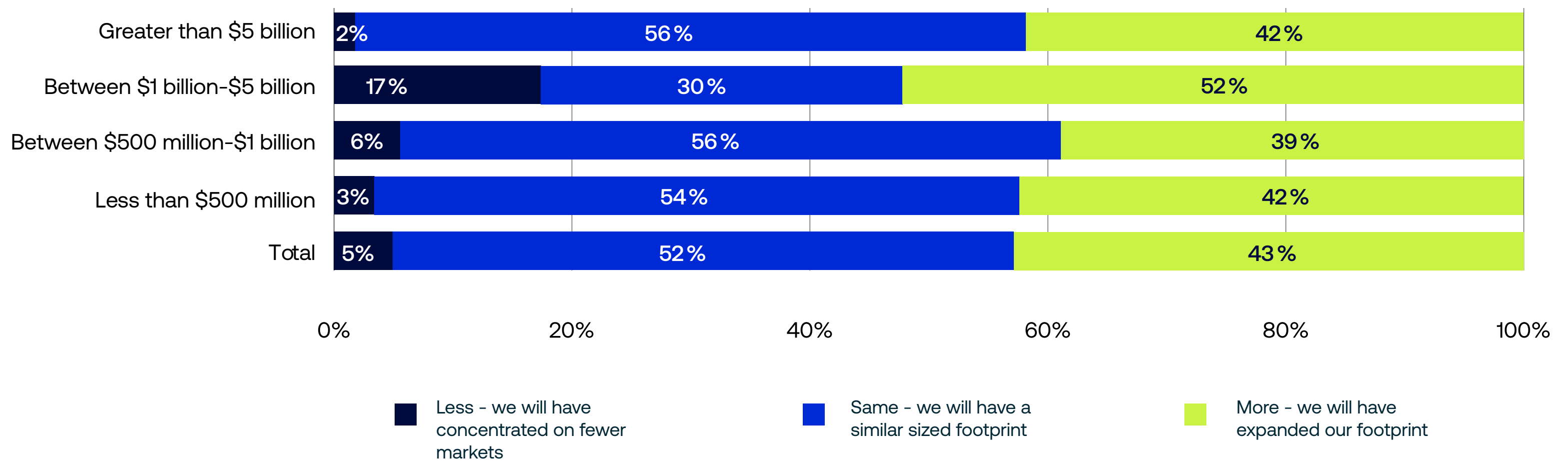




Note: Percentages represent the share of all responses, excluding “blank” or “not applicable” responses.

Geographic footprint expectations

A year from now, how many markets (metros, cities) do you think your firm / fund will be operating in?

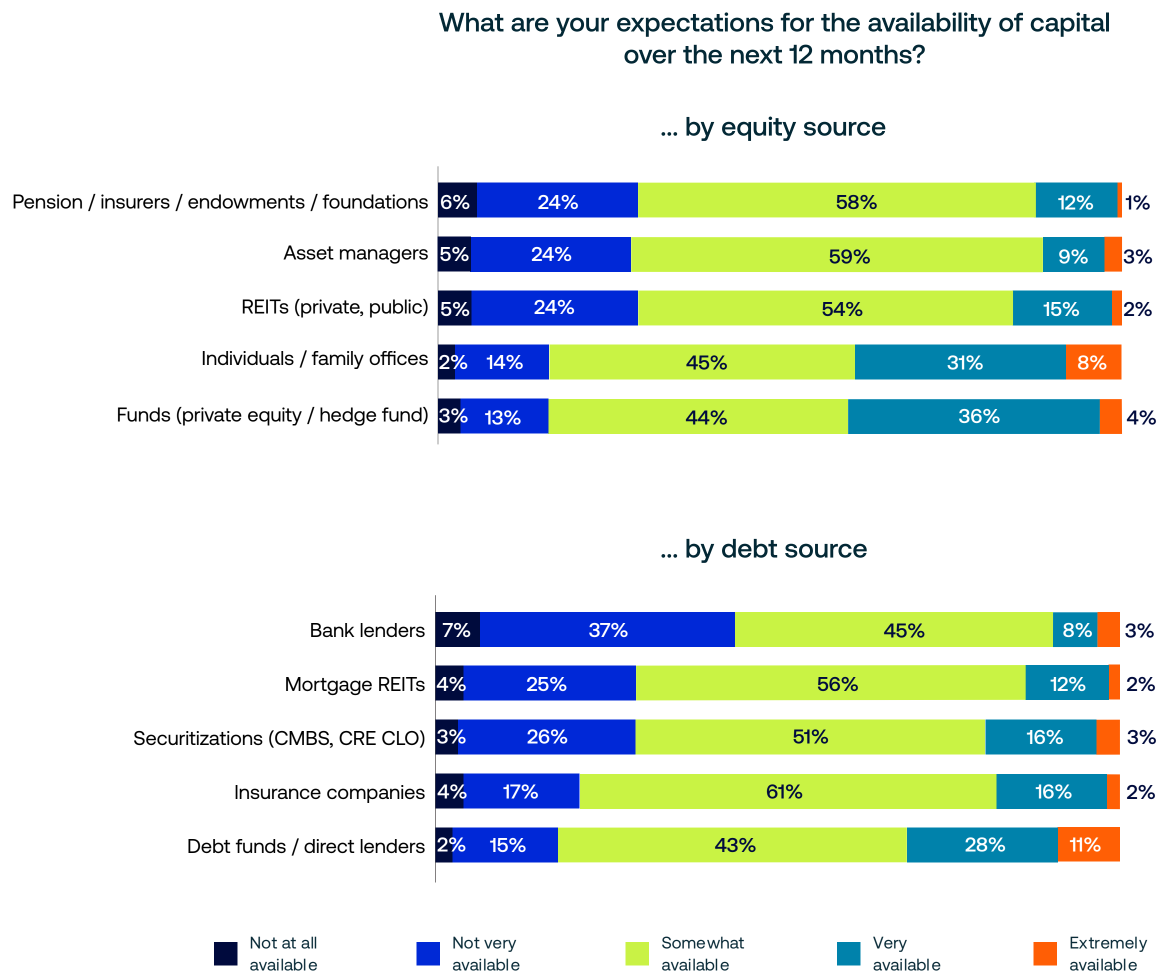


Note: Percentages represent the share of all responses, excluding “blank” or “not applicable” responses.

Capital availability

Capital availability expectations continue to improve across most sources except banks. Expectations for debt capital availability have improved dramatically across numerous sources versus the prior quarter. Net capital availability expectations (sum of responses for “extremely available” and “very available” less the sum of responses for “not very available” and “not at all available”) improved 20 percentage points for mortgage REITs, 22 percentage points for insurers, and 36 percentage points for securitizations. However, net expectations deteriorated rapidly for bank lenders, from -5% to -33% over the same period. Few respondents expect banks to return to CRE lending within the next 12 months, with 44% stating they expect banks to be “not at all available” or “not very available”.

Majorities say that they expect six of ten individual sources of capital to be “somewhat available” over the next 12 months while more than 40% of respondents reported the same for all ten. This is a signal that availability remains highly firm-, use case-, and/or relationship-specific.

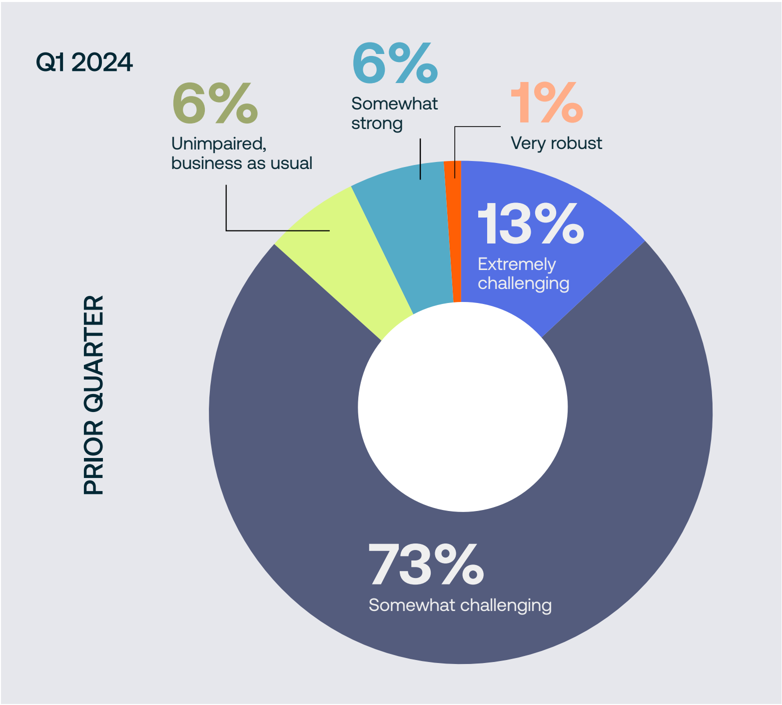


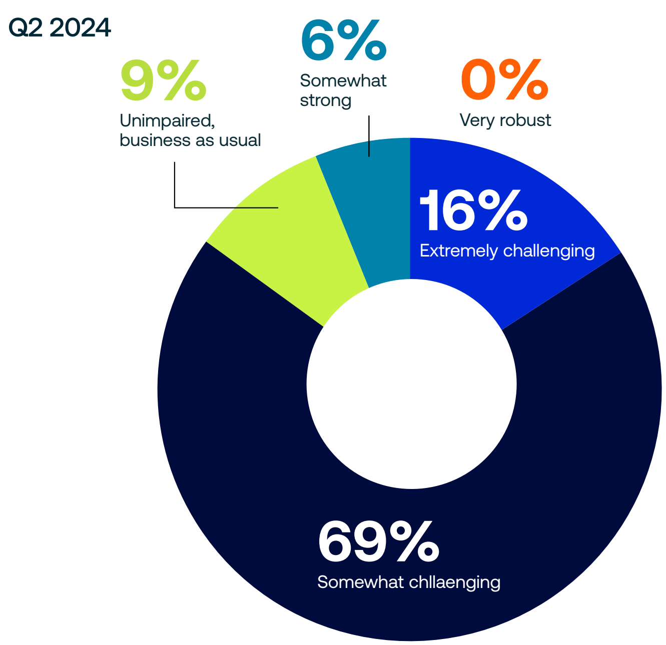
Note: Percentages represent the share of all responses, excluding “blank” or “not applicable” responses.

Expected operating environment

Marginal quarterly shifts as the operating environment is expected to remain broadly challenging. The percentage of respondents reporting that the coming months will be "challenging" remained nearly identical quarter-over-quarter (85% in Q2 2024 versus 86% in Q1 2024). However, expectations for the magnitude of said challenges have shifted slightly. The percentage of respondents who expect the operating environment to be "extremely challenging" ticked up just 3 percentage points to just 16% while those who believe it will be "somewhat challenging" decreased from 73% to 69%. Some respondents shifted to stating the environment may be "business as usual", with the fraction increasing from 6% to 9%.

What best describes your expectations for the operating environment over the next 12 months?





Note: Percentages represent the share of all responses, excluding "blank" or "not applicable" responses.

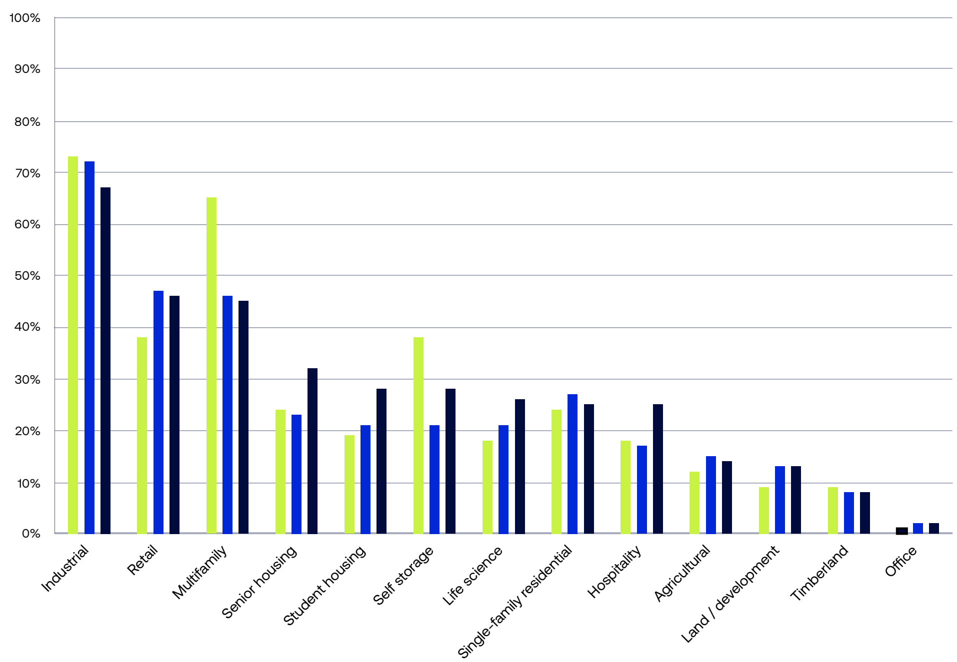
Expectations for property type performance

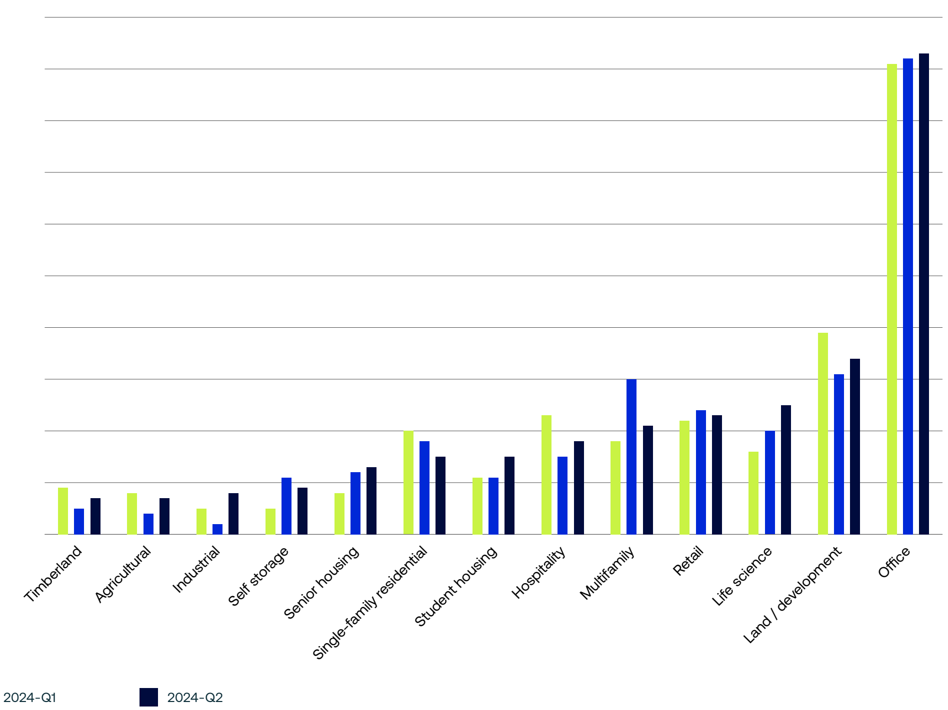
Expectations improve for all forms of housing, but wane for industrial. Survey participants still expect industrial to be the best-performing property type and office to be the worst over the next 12 months. Still, the former saw a notable decline in net favorability of 11 percentage points versus the prior quarter. Net expectations sentiment toward all forms of housing remained positive and improved quarter-over-quarter, with net expectations up 8 percentage points for multifamily and senior housing, up 3% for study housing, and up 1% for single-family residential. All other sectors experienced fewer than five percentage points of net sentiment shifts with the exception of self-storage, which improved 9% versus Q1 2024.

How to read the chart

The survey question asked participants to identify which property types they thought would be either "best" or "worst" performing in the next 12 months. Not all property types needed to be selected and any property type selected could only be identified as either "best" or "worst" performing, so no property could be identified as both "best" and "worst" performing. The percentages shown on the charts represent the share of respondents who included the property type as in either the "best" or "worst" performing categories.

Rank which property types you expect to be the best and worst performing in the next 12 months.

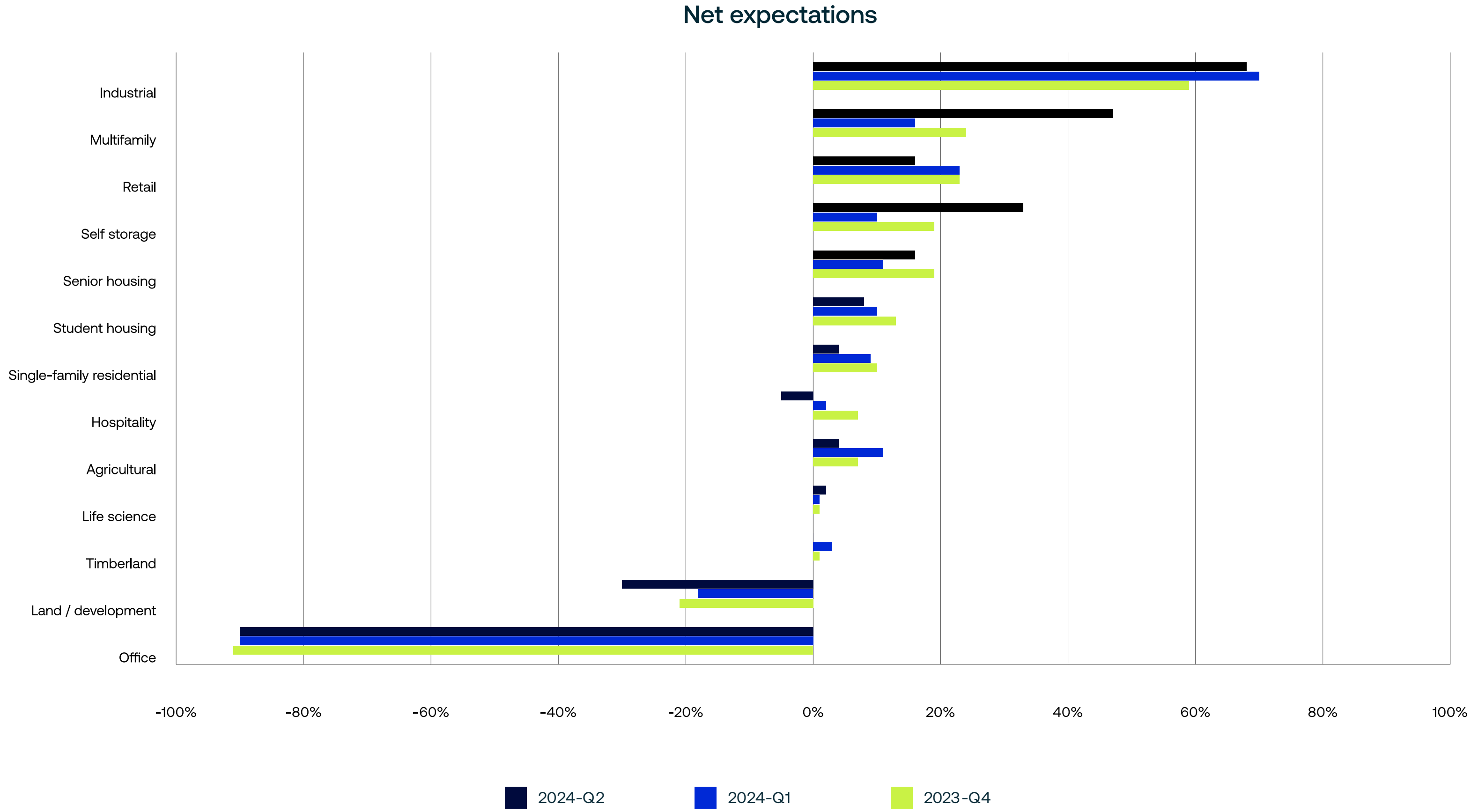




Note: Percentages represent the share of all responses, excluding "blank" or "not applicable" responses.

Expectations for property type performance

Rank which property types you expect to be the best and worst performing in the next 12 months.



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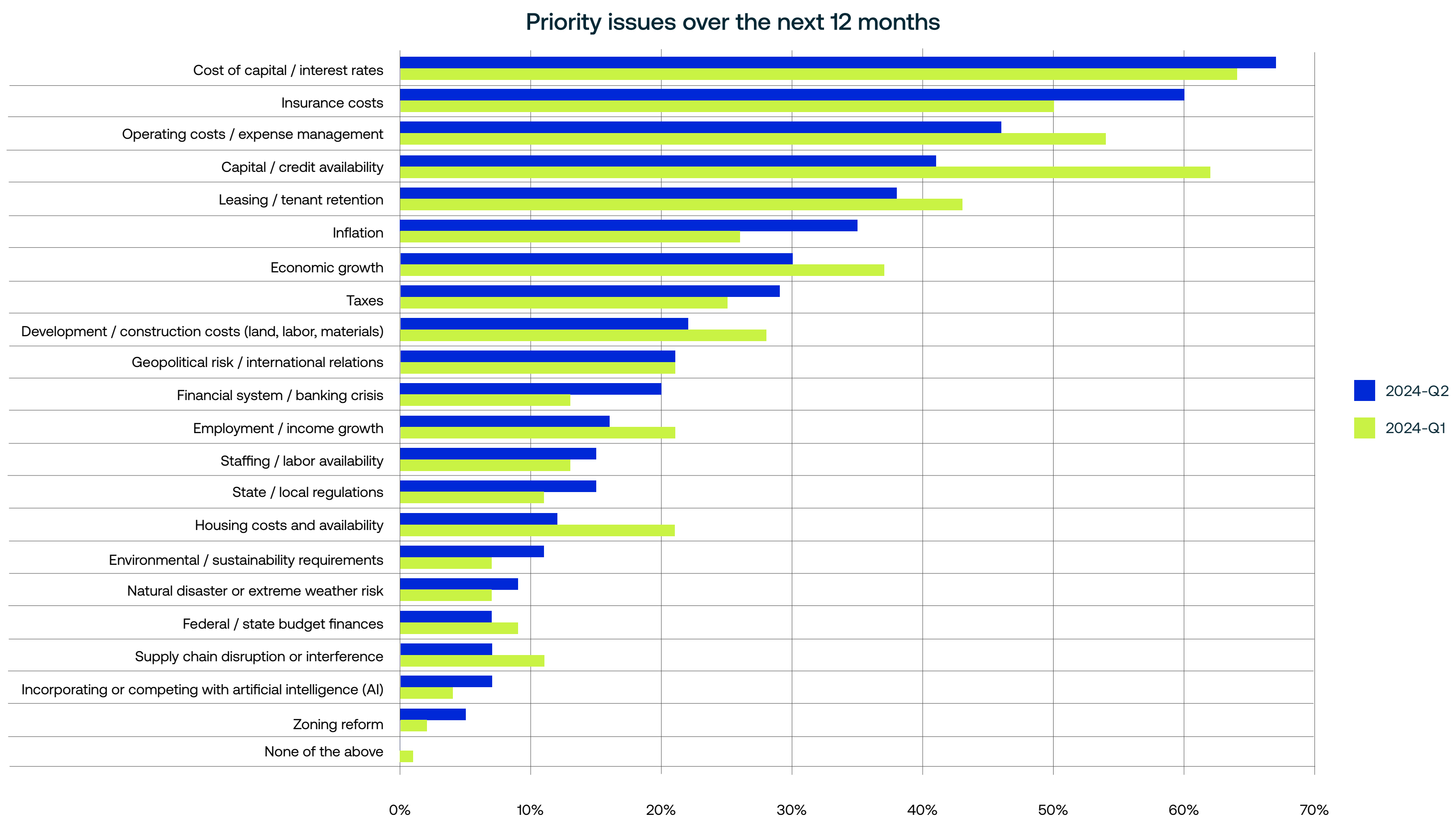
Note: Percentages represent the share of all responses, excluding "blank" or "not applicable" responses.

Priority issues over the next 12 months

Costs dominate near-term priorities; capital availability concerns plummet. Similar to the previous quarter, the cost of capital remained the top concern of respondents, with 67% marking it as a priority over the next 12 months. Insurance costs followed with six in ten marking it as a top priority. Property-specific concerns waned quarter-over-quarter, with operating costs being the top concern of 46% of respondents versus 54% in Q1 2024, and leasing/ tenant retention being the top concern of 38% of respondents (down from 43% in Q1 2024). Capital availability concerns saw the largest change quarter-over-quarter, plunging more than 20 percentage points from being a top concern of more than 60% of respondents to just over 40%. Geopolitical risk continues to be a concern, remaining a top priority of more than one in five respondents for the third consecutive quarter.



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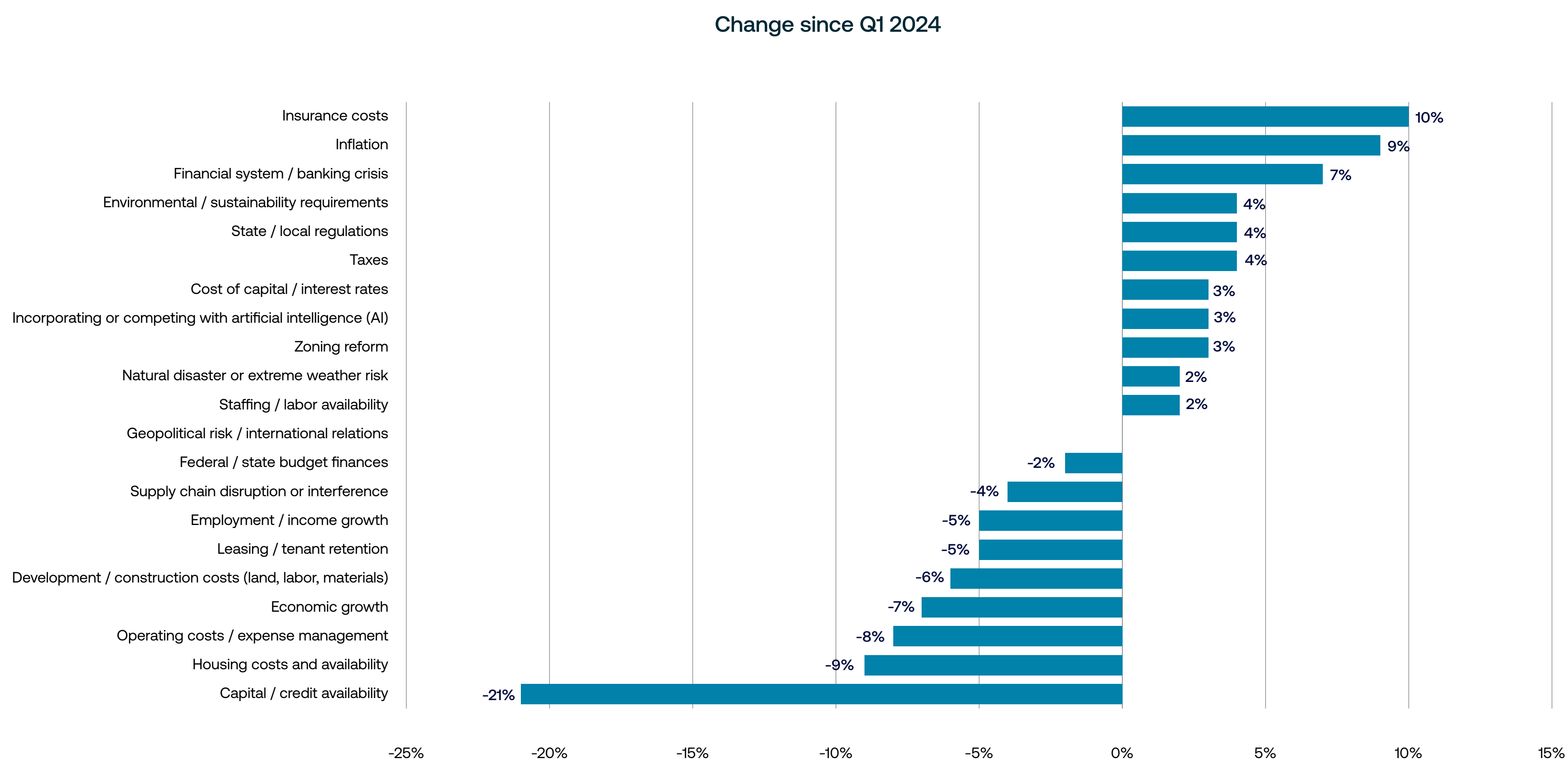
Priority issues over the next 12 months

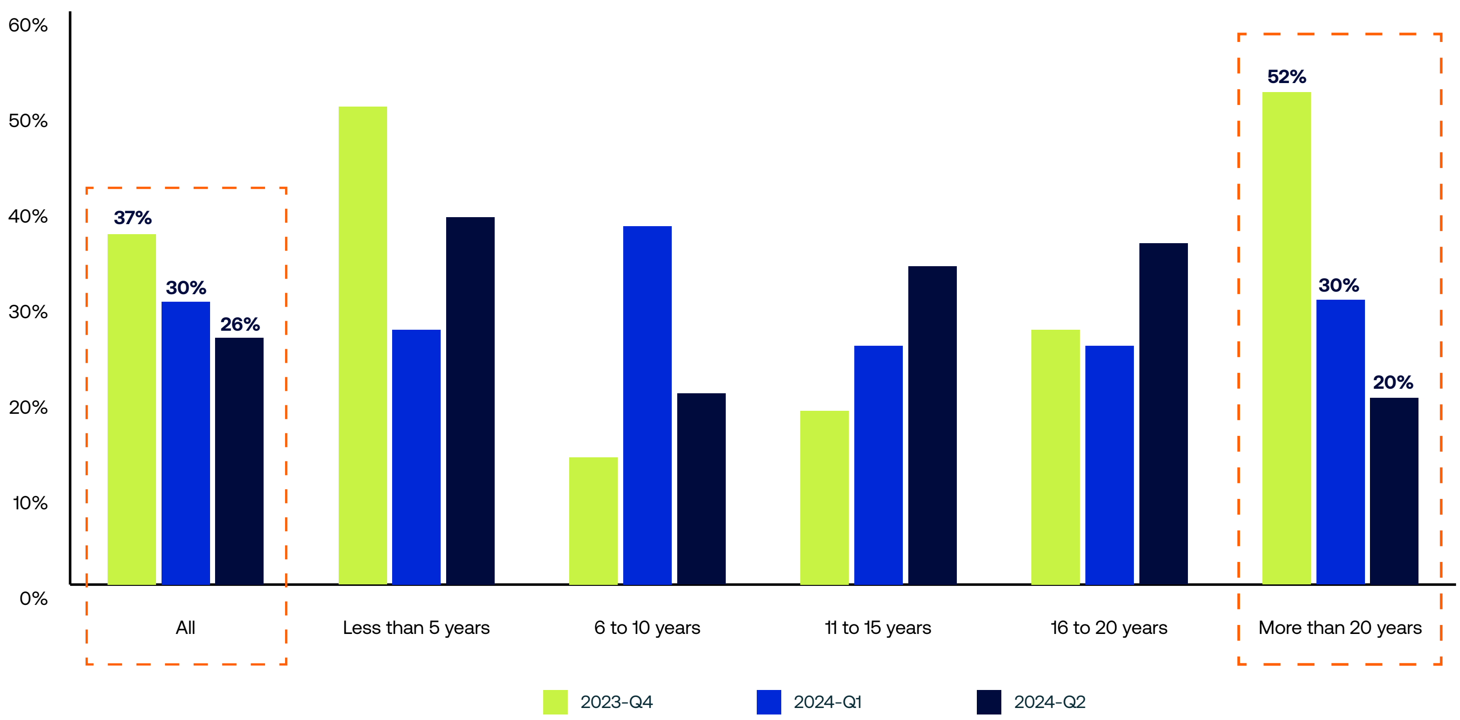


Note: Percentages represent the share of all responses, excluding “blank” or “not applicable” responses.

Artificial Intelligence (AI)

AI skepticism is dropping, driven by rapid acceptance among tenured professionals. Just one in five CRE professionals with greater than 20 years of experience view artificial intelligence as an "unproven technology" with unknown benefits to the CRE industry. As recently as Q4 2023, more than half of this same cohort expressed skepticism of the technology. Less experienced professionals, particularly those with fewer than 5 years in the industry, remain skeptical with 38% reporting that the technology as having unknown benefits for CRE.

Percentage of CRE professionals who believe "AI is unproven technology", by years of experience



Note: Percentages represent the share of all responses, excluding "blank" or "not applicable" responses.

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