MARKET UPDATES
COVID-19 Impacts on U.S. Commercial Real Estate
May 15, 2020

WEEK IN REVIEW
Economic Outlook Takes Negative Turn; Real Estate Shows Signs of Life

- U.S. economic forecasts took a negative turn this week, overshadowing a bounce back in China.
- A significant decline in office leasing activity is placing downward pressure on net effective rents.
- Sustained leasing activity and low vacancies are creating attractive opportunities for industrial investors.
- Inertia prevails in the retail sector as tenants and investors wait to gauge the business climate after reopening.
- Multifamily remains resilient, with strong rent collections in early May, but average rents are slightly lower and investment volume is muted.
- The hotel sector is at a standstill; an early economic recovery is critical for this sector to regain traction and maintain liquidity.
- Data centers continue to pick up momentum from growing demand, although capital markets activity is muted.
- In Asia Pacific, New Zealand appears well on the road to recovery after easing lockdown restrictions and reopening 90% of its economy this week. However, the toll on 2020 GDP will be significant.

ECONOMY
Weakened Outlook

Fed Chairman Jerome Powell called for further government fiscal stimulus to help prevent a prolonged recession. Government stimulus to date totals nearly $3 trillion or 11% of GDP. The House proposed another $3 trillion package this week, but it is unlikely to pass the Senate as currently proposed. Ultimately, we believe Congress will agree to another round of at least $2 trillion in some form. CBRE’s current forecast is for unemployment to peak at 15% and fall to around 9% by year’s end. Other economists are more pessimistic, with Goldman Sachs forecasting unemployment at 25% in Q2. Meanwhile in China, there are signs of an apparent economic bounce back. CBRE’s real-time economy trackers suggest that GDP growth has returned in China to about 4% on an annualized basis.
OFFICE
Stalled

Office leasing and capital markets activity generally have remained stalled as continued economic uncertainty plagues markets, work-from-home policies continue and occupiers reassess their needs for space. Total U.S. leasing activity in April was under 8 million sq. ft.—less than half the monthly average. Rents held steady, partly due to higher concessions, but are at risk of falling. Manhattan reported a significant decline in asking rents. However, some markets, mostly in the Sun Belt, reported a noticeable uptick in leasing inquiries over the past week. Office sales transactions also remain stalled, hampered by the uncertain economic outlook and lack of clarity on underwriting assumptions.

INDUSTRIAL
Solid

Industrial leasing activity was solid in April, as many deals negotiated before the COVID-19 crisis were closed. While the market is expected to remain active, leasing will shift to more short-term new deals and longer-term renewals. Overall taking rents have remained stable due to low vacancies, with reductions only for smaller-sized flex facilities. However, landlords generally appear willing to increase concessions, including free rent, which are lowering net effective rents. Sale prices have not been affected, as investors consider industrial the safest commercial asset class for both the short and long terms. Institutional capital is actively looking for opportunities in both core and emerging markets.

RETAIL
Stagnant

Leasing and capital markets activity remains minimal, as most tenants and investors await consumer response once closed stores are reopened. While there has been a slight shift in leasing sentiment, indicating that tenants and landlords want to return to the negotiating table, actual deals largely will not take place until new structures are determined. Capital markets activity has been focused on smaller deals and triple-net properties, especially those occupied by essential retail tenants. Too much economic uncertainty and a lack of price transparency remain for larger transactions to take place.

MULTIFAMILY
Relative Strength

Multifamily rent collections in May were slightly ahead of April and only 1.5 percentage points less than a year ago. The National Multifamily Council reported an 80.2% collection rate this month as of May 6, compared with 78% in April and 81.7% a year ago. Owners are reporting a pick-up in new leasing activity, though still far lower than a year ago. Retention rates remain higher than normal. Rents on renewals are flat to slightly positive; rents on new leases are lower than the pre-COVID-19 period. Average asking rents are down 1% since March 11. Investment activity is at reduced levels. March closings fell 23% from a year ago; April could register a decline of more than 50%.
HOTELS
Timing Critical

Hotel transaction activity remains at a standstill as the bid/ask spread is wide. Only spot-liquidity trades are likely for now. Occupancy levels remain in the mid-20% range and industrywide ADRs have fallen by more than 40% year-over-year. Most owners have short-term liquidity through either strong balance sheets, government assistance or forbearance. However, recovery timing is critical and, if prolonged, will compound the stress on liquidity.

DATA CENTERS
Growing Demand

Leasing activity remained strong across data center markets in April, highlighting continued momentum of the sector. Several megawatts were absorbed, largely by cloud providers who continue to meet growing demand. Capital markets, however, had a slower month and did not see much movement. Prices remained steady across the country, though fell for lower-credit leasebacks as financing dried up.

ASIA PACIFIC
New Zealand Reopens

After successfully halting the spread of COVID-19, New Zealand eased its lockdown restrictions and reopened 90% of its economy this week. Despite this positive news, the economic cost of the lockdown, combined with New Zealand’s comparatively heavy reliance on tourism, has been substantial. Fiscal stimulus of approximately 10% of GDP and a massive quantitative easing program have failed to change many forecasts of a steep GDP decline in 2020. Landlords and tenants continue to make rent payments the main short-term priority. The market norm appears to be a 50% reduction on net rent only, with no relief for operational expenditure.

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