

CBRE ECONOMETRIC ADVISORS Presents

# NEW LANDSCAPE

CBRE AMERICAS RESEARCH CONFERENCE 2017

## CAPITAL MARKETS OUTLOOK

*SPENCER LEVY  
SERGUEI CHERVACHIDZE  
RICHARD BARKHAM*

SEPTEMBER 14, 2017



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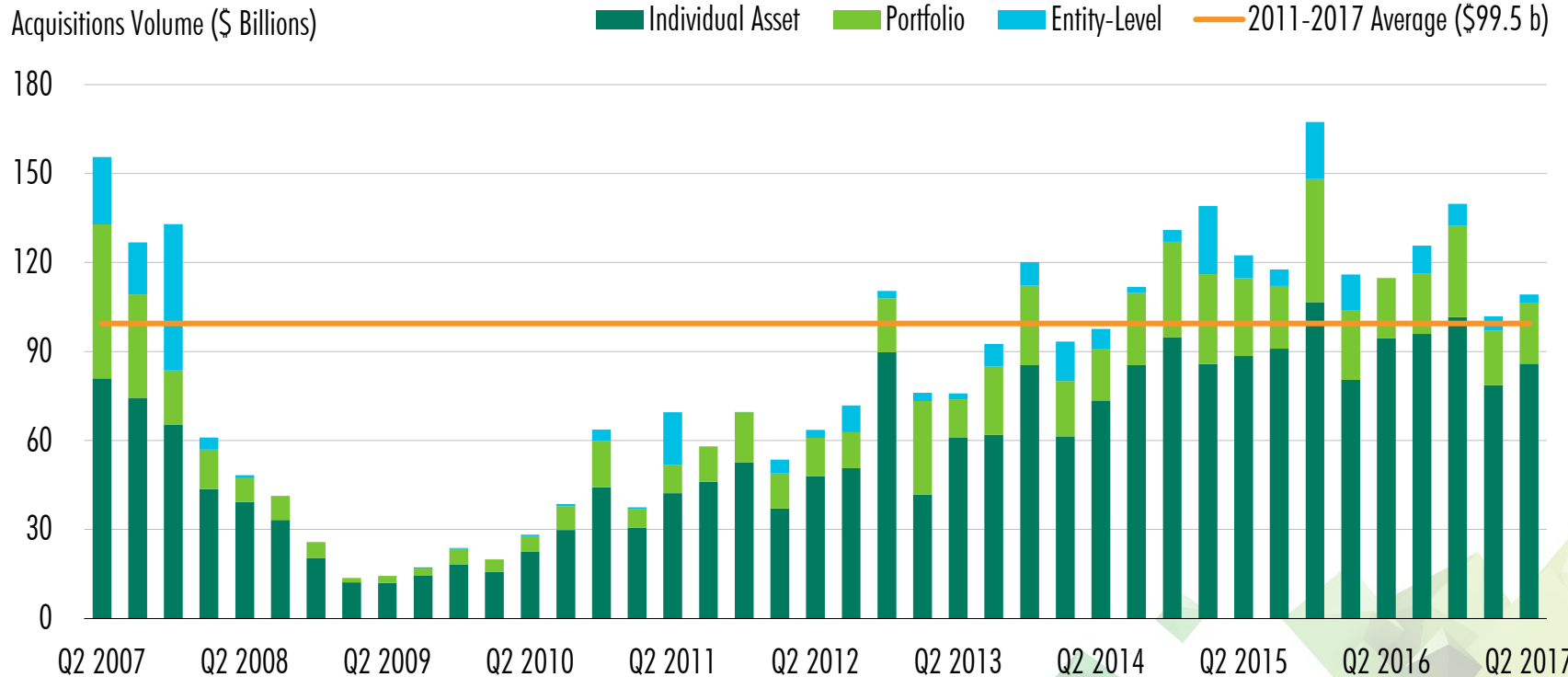
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## CAPITAL MARKETS 2017 MID-YEAR REVIEW

*SPENCER LEVY | SENIOR ECONOMIC ADVISOR |  
AMERICAS HEAD OF RESEARCH*

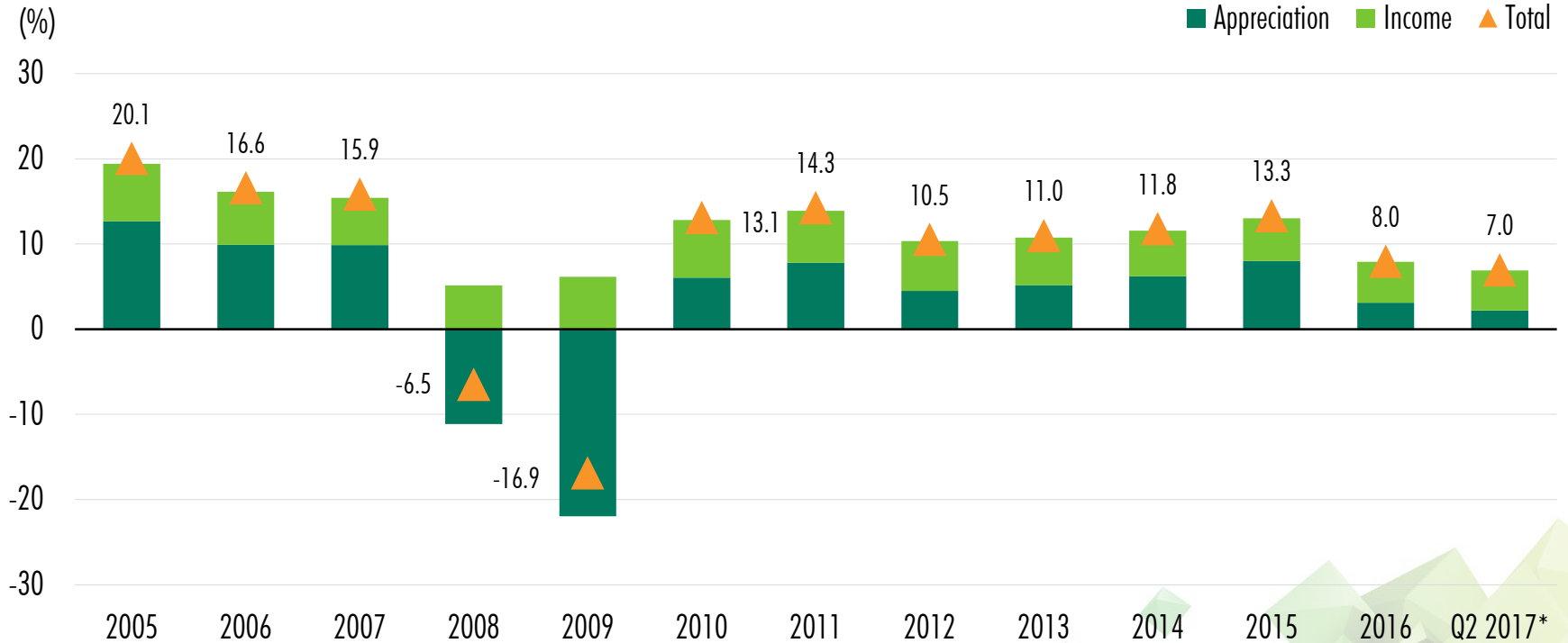
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# DEAL VOLUME: AVERAGE IS THE NEW GOOD?



Source: CBRE Research, Real Capital Analytics, Q2 2017.

# 7% RETURNS: THE NEW NORMAL?



Source: CBRE Research, NCREIF, Q2 2017.

\*For year ending Q2 2017. All returns are reported on an unlevered basis.

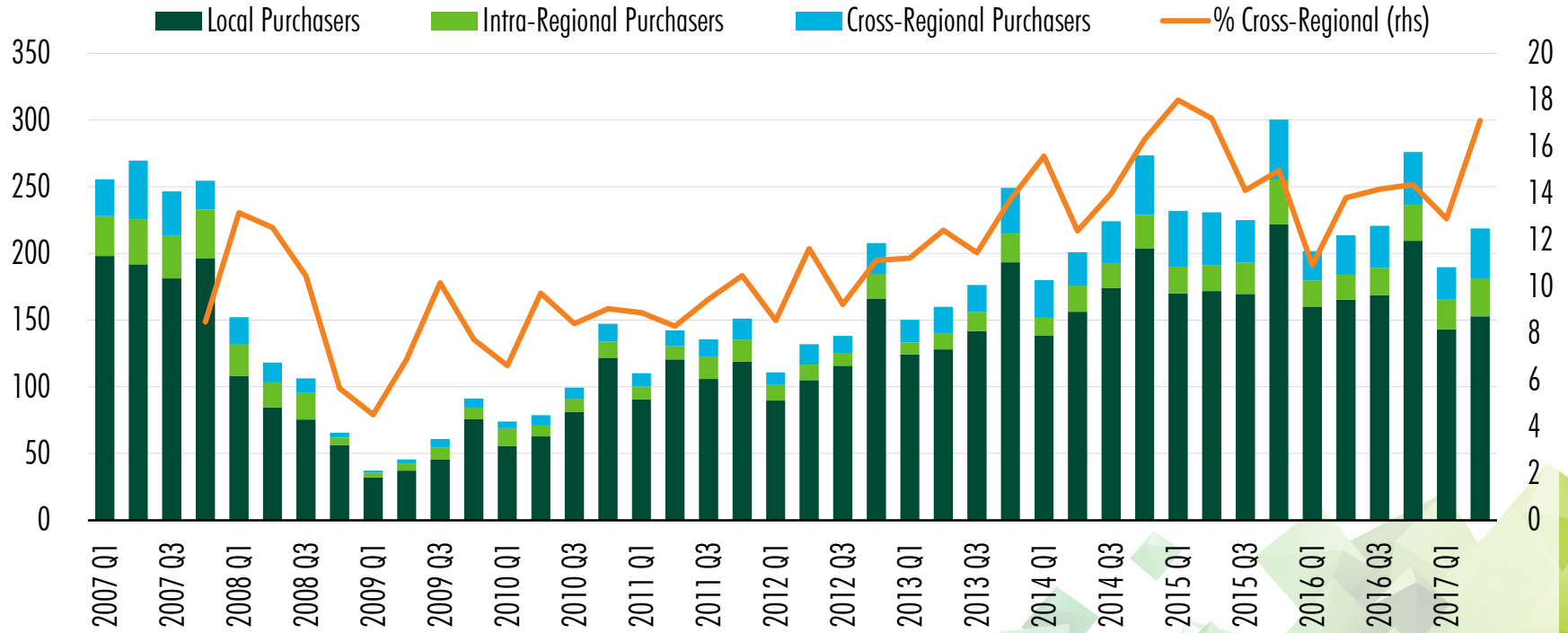
# WITH EQUITY MARKETS UNCERTAIN, DEBT LOOKS MORE ATTRACTIVE

Key Underwriting Measures	Q2 2017	Q1 2017	Q2 2016
Debt Service Coverage Ratio	1.52	1.51	1.51
Loan-to-Value (LTV) (%)	65.5	65.4	66.3
Cap Rate (%)	6.26	6.22	6.31
Amortization Rate (%)	19.2	24.0	24.4
Percent Partial or Full Interest-Only	58.7	55.6	57.4
Percent Full Interest-Only	17.8	11.1	11.2
Loan Constant (%)	6.19	6.23	5.96
Interest Rate (%)	4.30	4.24	4.09
Debt Yield (%)	9.96	9.93	10.05

Source: CBRE Research, Q2 2017.

Note: Amortization rate reflects the average percentage of origination balances scheduled to pay down over the loan term.

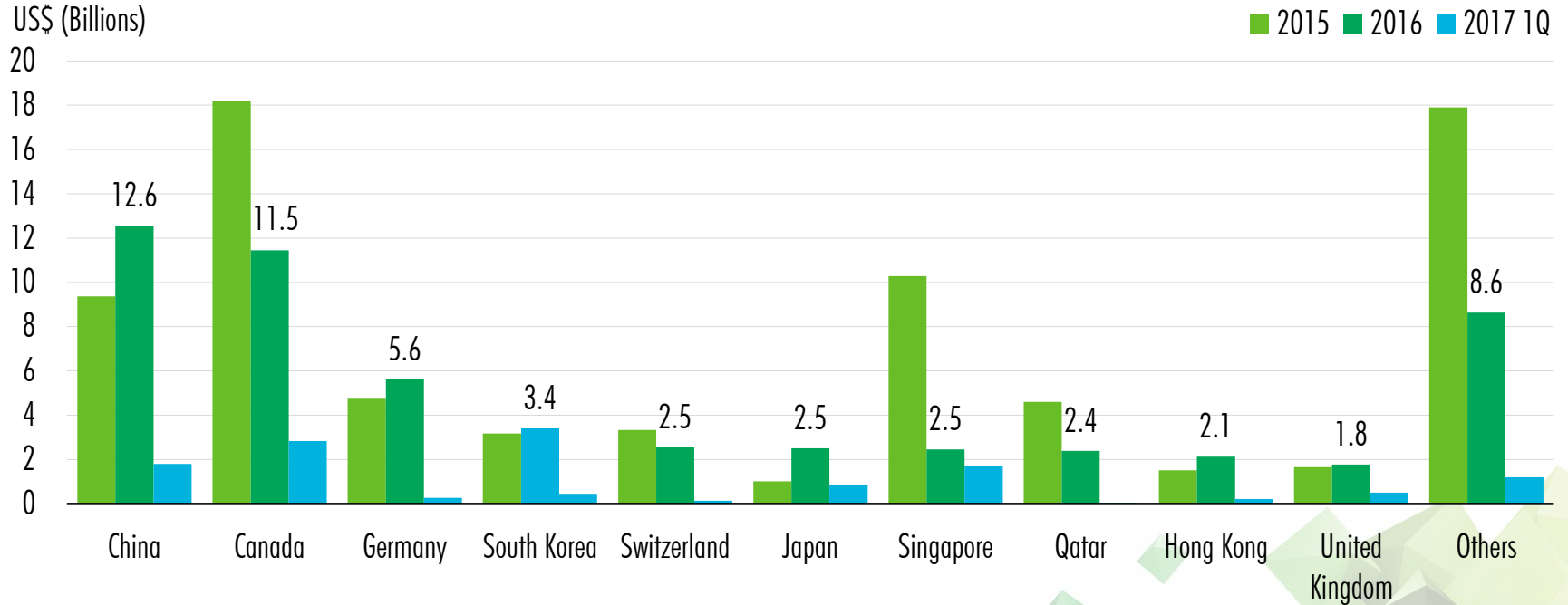
# DESPITE CHINA, GLOBAL CRE INVESTMENT WILL CONTINUE TO INCREASE



Source: CBRE Research, Real Capital Analytics, Q2 2017.

# LARGEST FOREIGN INVESTORS INTO U.S.

## U.S. INBOUND INVESTMENT BY SOURCE OF CAPITAL

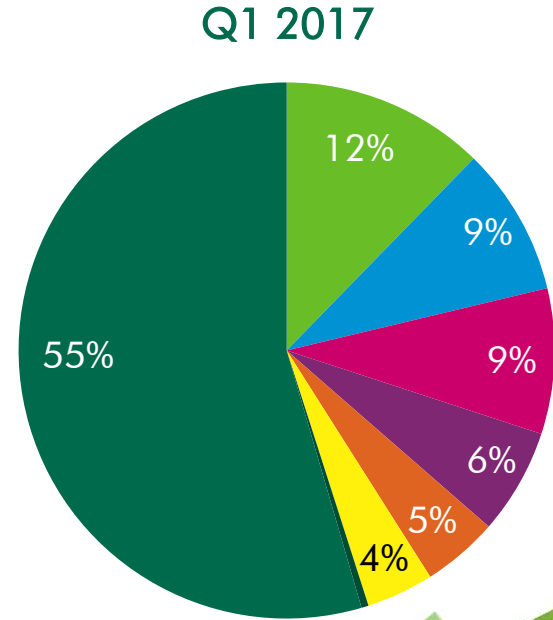
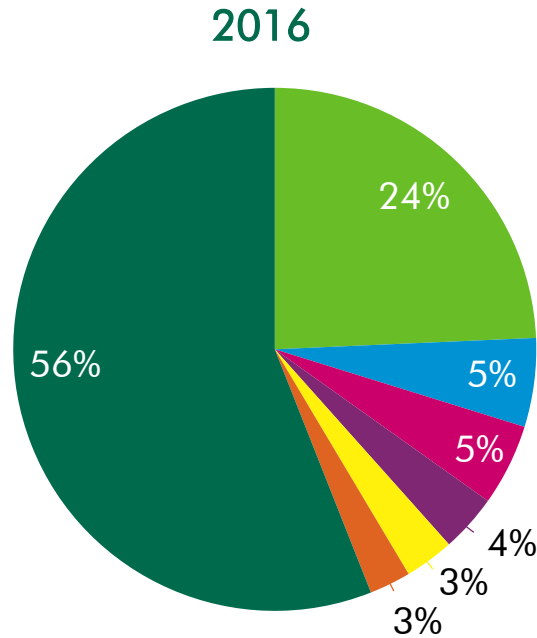


Note: Transactions include deals in the Office, Retail, Industrial, Hotel, Residential and Other commercial sectors. Development sites are excluded.

Source: RCA, CBRE Research

# TOP INVESTMENT DESTINATIONS

- New York
- San Francisco
- Los Angeles
- Washington
- Chicago
- Boston
- Other Gateway
- Non-Gateway



Note: Transactions include deals in the Office, Retail, Industrial, Hotel, Residential and Other commercial sectors. Development sites are excluded.

Source: RCA, CBRE Research, June 2017.



# TOP INVESTMENT DESTINATIONS

“WHICH METRO IN THE AMERICAS DO YOU BELIEVE TO BE THE MOST ATTRACTIVE FOR PROPERTY INVESTMENT PURCHASE?”

**#1 LOS ANGELES (5<sup>TH\*</sup>)**

**#2T NEW YORK (4<sup>TH</sup>)**

**#2T DALLAS/FT. WORTH (1<sup>ST</sup>)**

**#4 SEATTLE (7<sup>TH</sup>)**

**#5 WASHINGTON, D.C. (8<sup>TH</sup>)**

**#6 ATLANTA (6<sup>TH</sup>)**

**#7 HOUSTON (14<sup>TH</sup>)**

**#8 SAN FRANCISCO (4<sup>TH</sup>)**

**#9 BOSTON (10<sup>TH</sup>)**

**#10 CHICAGO (3<sup>RD</sup>)**

**#11 AUSTIN (15<sup>TH</sup>)**

**#12 DENVER (17<sup>TH</sup>)**

\*In parentheses: Rank in 4-year forecast for office-using job growth.

Source: CBRE Research, Global Investor Intentions Survey 2017, CBRE Econometric Advisors

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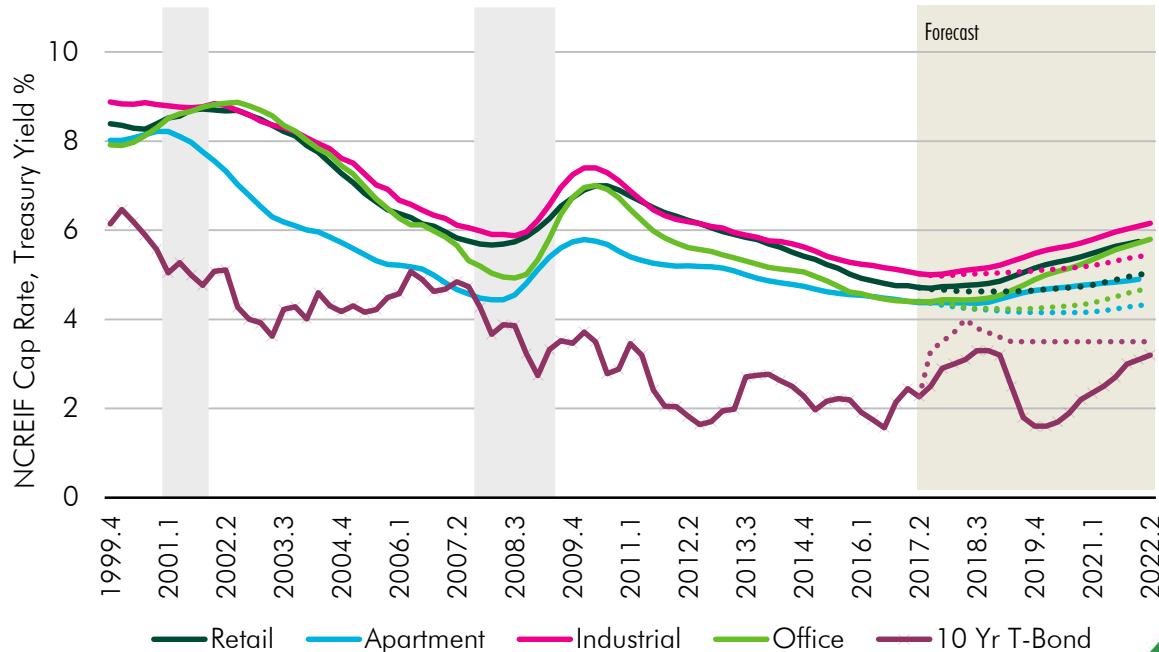
## CAPITAL MARKETS: UP OR DOWN? ASSET PRICING, GOING FORWARD

*SERGUEI CHERVACHIDZE, PH.D.  
AMERICAS HEAD OF FORECASTING*

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# WHITHER CAP RATES?

## NCREIF NPI Capitalization Rates: Baseline vs. High Interest Rates Scenario (Dashed)



- Cap rates are at risk of upward adjustment under both scenarios
- *Baseline*: Cap rates increase in spite of Fed easing, as risk premiums spike during mild recession

Eventually, cap rates stabilize and risk premiums return to long-run trend levels

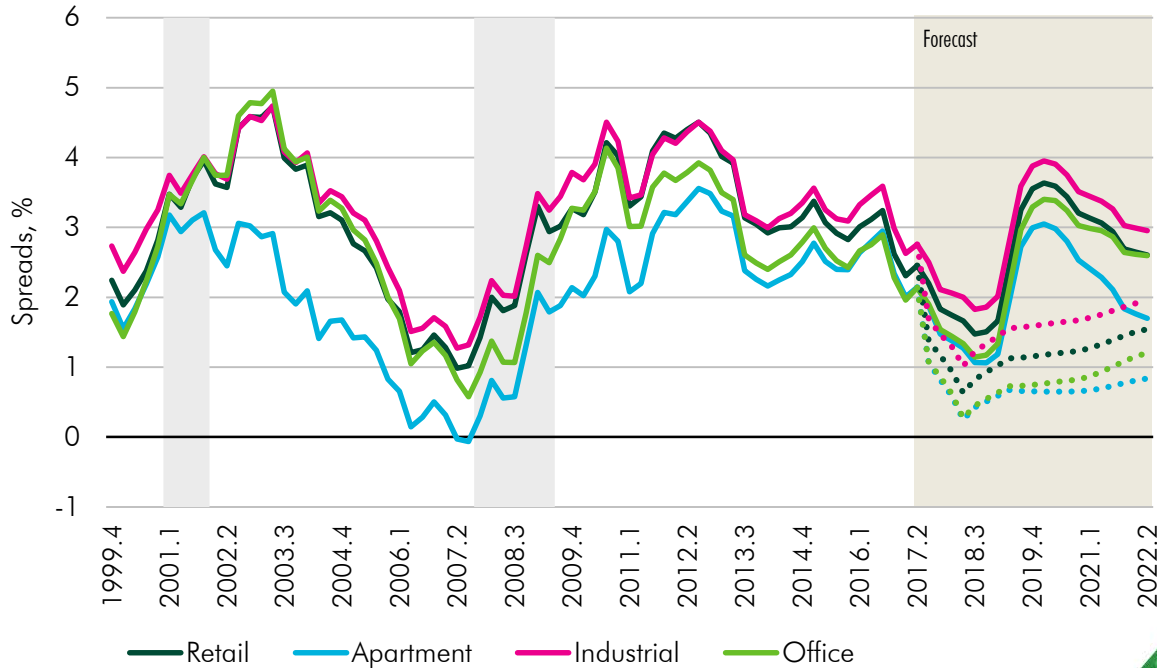
- *High Interest Rates*: Cap rates initially stay flat in spite of bond yield increases, as strong NOI growth is priced aggressively

As growth slows, cap rates begin to increase moderately as asset prices adjust in response to lower NOI growth expectations

Sources: NCREIF, CBRE Econometric Advisors, Q2 2017.

# WHITHER SPREADS?

Spread over 10-Year Treasury Yield, NCREIF NPI Capitalization Rate: Baseline vs. High Interest Rates Scenario (Dashed)



- Baseline:* Cap rate spreads spike significantly as a result of mild recession

Spreads do not reach 2009-crisis levels, however

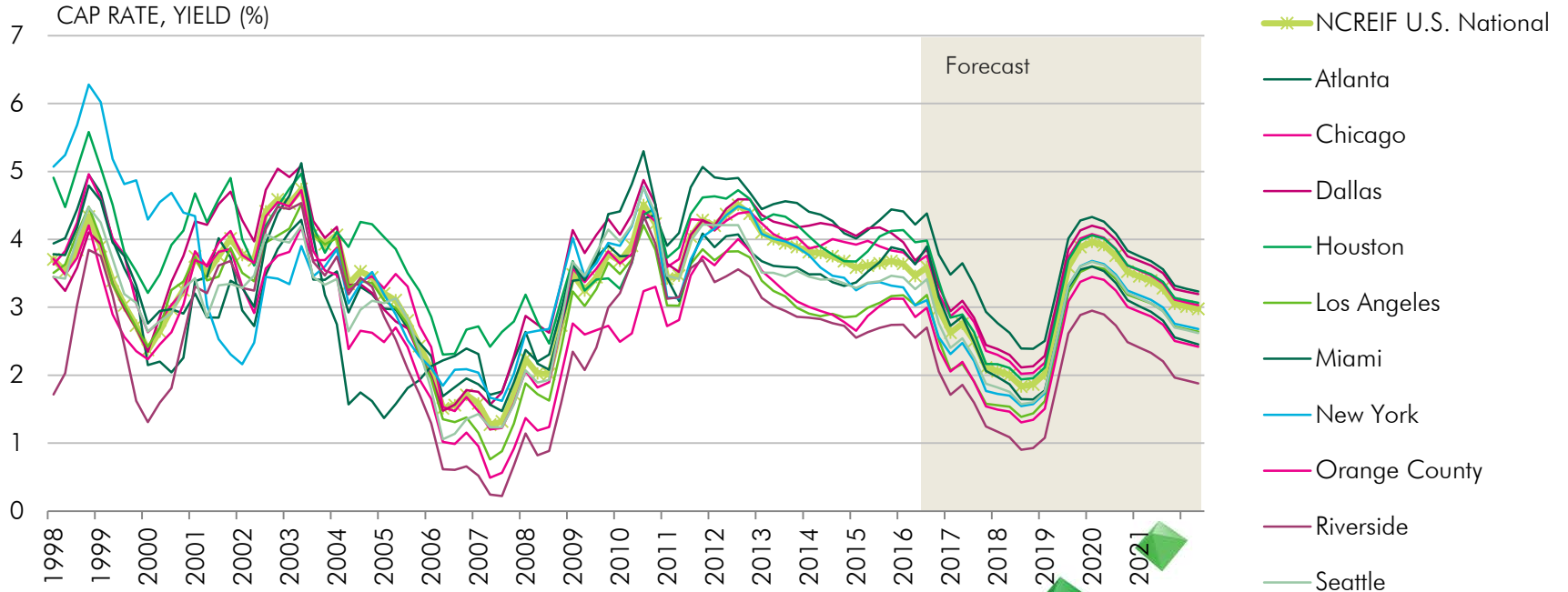
As economy recovers, spreads trend downward to long-run levels
- High Interest Rates:* Spreads compress at first, as high-growth expectations encourage aggressive pricing while cap rates stay flat despite interest rate increases

As growth slows, income expectations moderate, assets are repriced and spreads trend toward long-run levels

Sources: NCREIF, CBRE Econometric Advisors, Q2 2017.

# ASSET PRICING WILL VARY BY MARKET

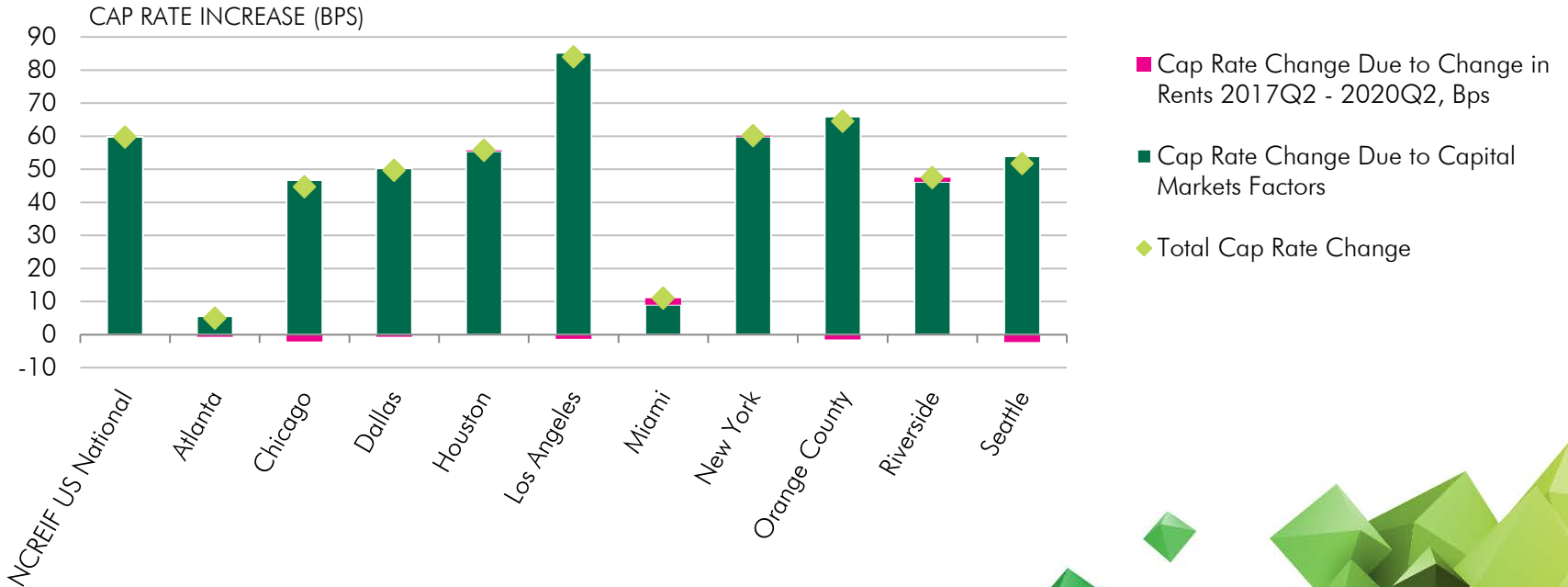
Spread of U.S. Industrial Cap Rates over 10-year T-Bond Yield: Top 10 Markets



Sources: NCREIF, CBRE Econometric Advisors, Q2 2017.

# ASSET PRICING WILL VARY BY MARKET

Industrial: Decomposing Cap Rate Increases: Rent Change vs. Capital Markets Effects, Q2 2017 – Q2 2020



Sources: NCREIF, CBRE Econometric Advisors, Q2 2017.

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## CAPITAL FLOWS: WHERE NEXT?

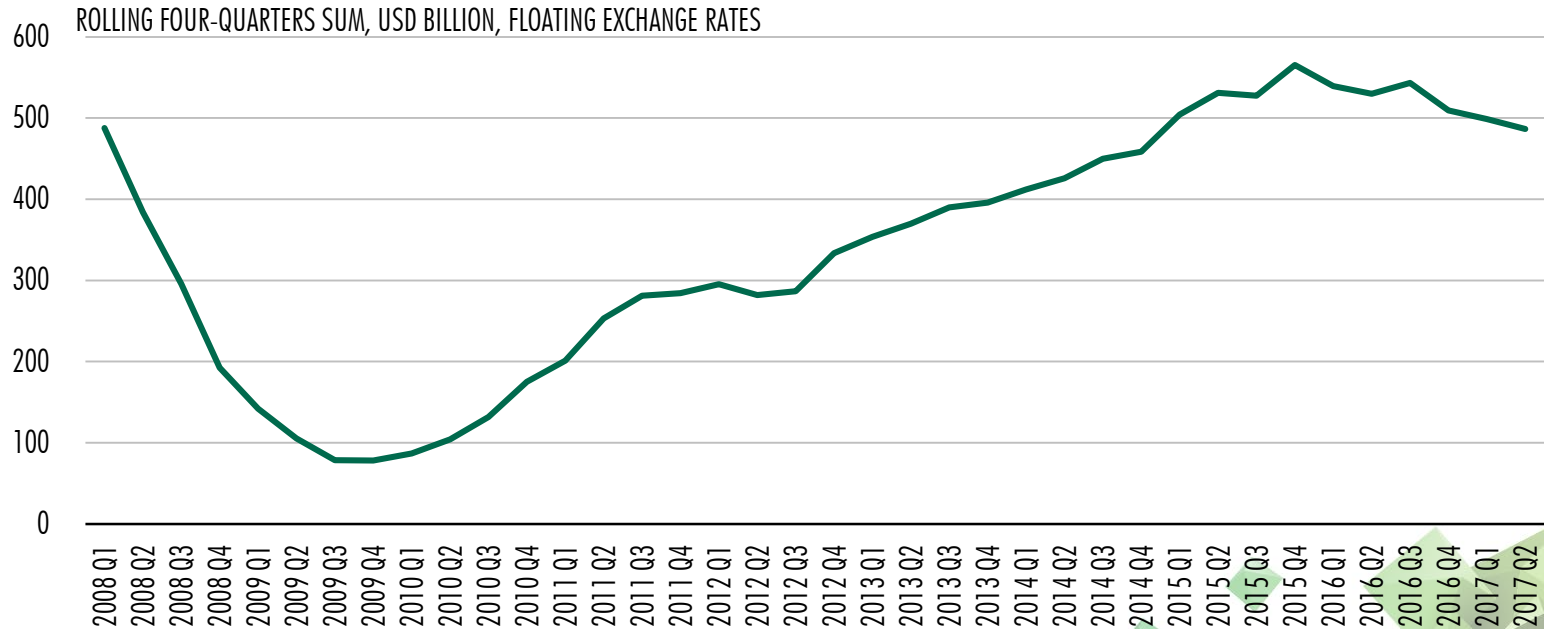
*RICHARD BARKHAM, PHD MRICS CRE,  
GLOBAL CHIEF ECONOMIST*

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# CAPITAL FLOWS INTO U.S. REAL ESTATE (ROLLING ANNUAL)

## Capital Flows into U.S.

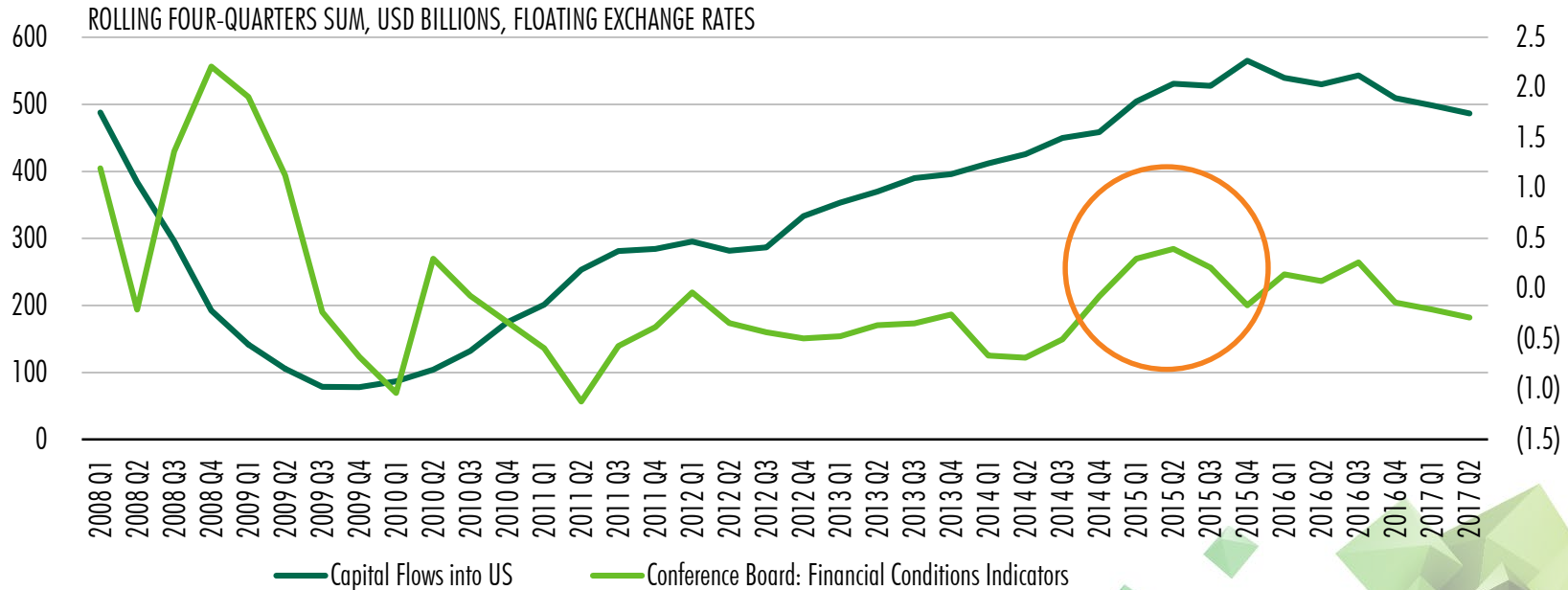


Source: CBRE Research, Real Capital Analytics, Q2 2017.



# FINANCIAL CONDITIONS WORSENEDED IN 2015

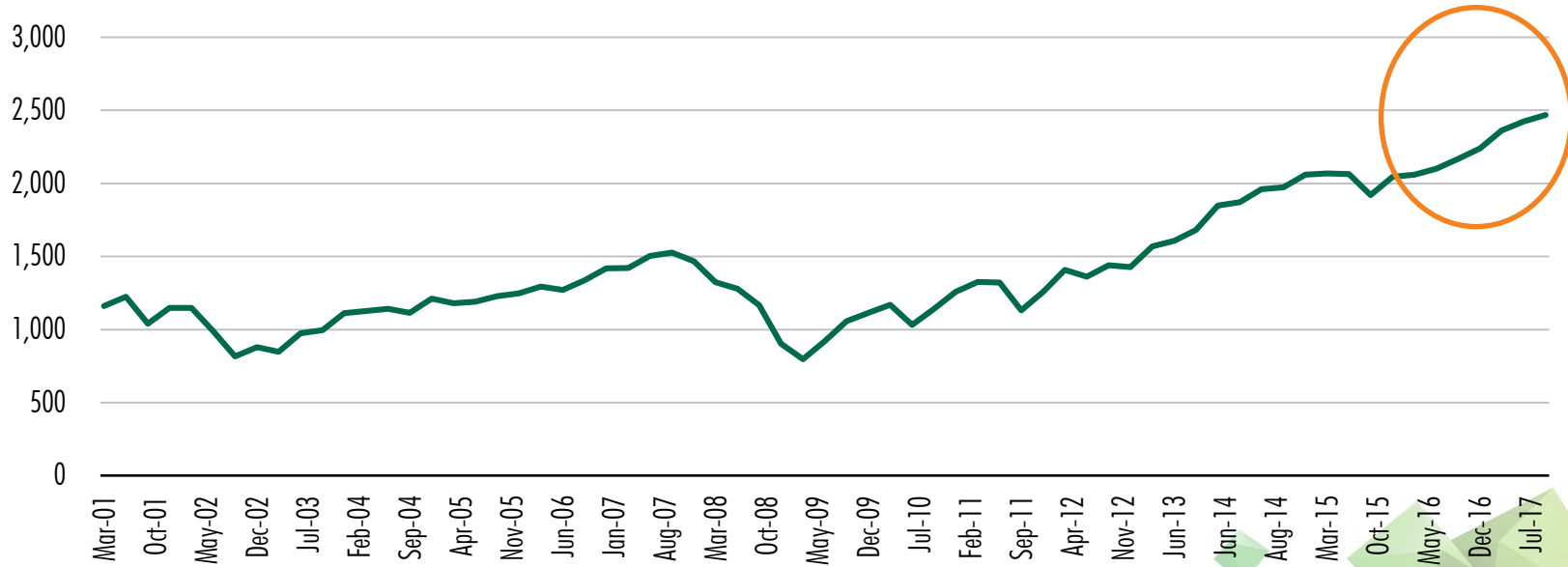
## Financial Condition Indicators and Capital Flows into the U.S.



Source: CBRE Research, Conference Board, Q2 2017.

# U.S. STOCKS ARE DOING WELL

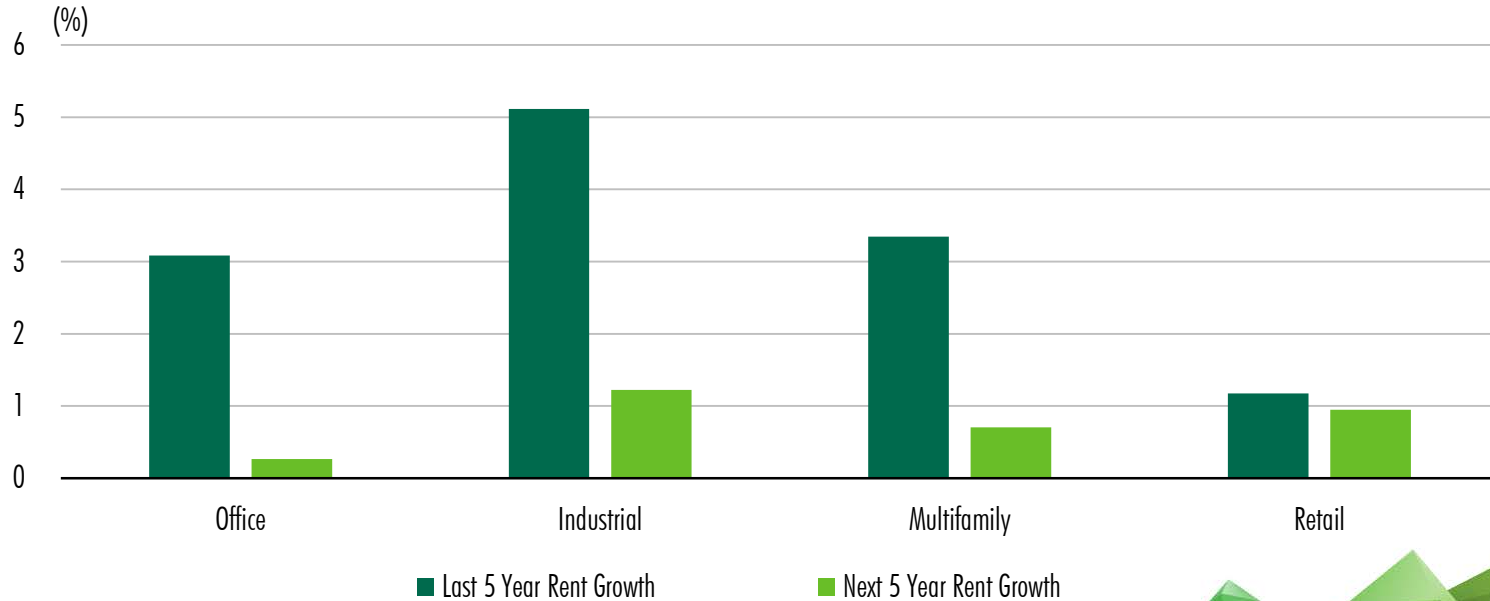
## S&P 500 Index



Source: CBRE Research, Bloomberg Market, September 2017.

# RENTAL OUTLOOK NOT AS PROMISING

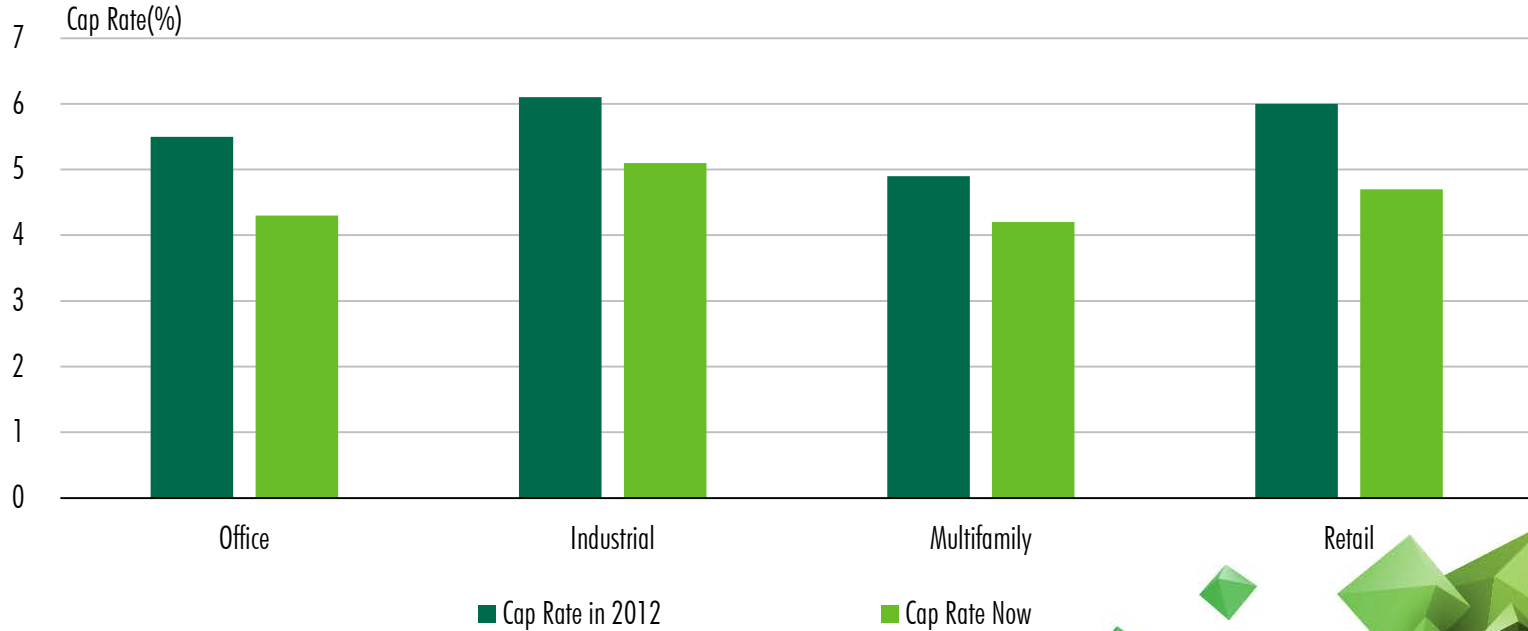
## U.S. Rent Growth



Source: CBRE Research, CBRE EA, Q2 2017.

# CAP RATES LOWER

## Cap Rate Comparison



Source: CBRE Research, CBRE EA, Q2 2017.

# RETURNS VS HURDLE

## Notional Total Return and Hurdle Rate



Source: CBRE Research, CBRE EA, Q2 2017.

# THANK YOU

# CAPITAL MARKETS

# OUTLOOK

*SPENCER LEVY | SENIOR ECONOMIC ADVISOR  
AMERICAS HEAD OF RESEARCH*

*SERGUEI CHERVACHIDZE | SENIOR ECONOMIST, AMERICAS  
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