nyrej

# After the pandemic: Should you invest in CRE? - by Vladislav Poshmorga

May 18, 2021 - New York City

If you asked a financial or industry analyst in October 2020 to predict the state of commercial real estate in the U.S., they probably would have forecasted that property prices would decline 10% to 15% as the COVID-19 Pandemic raged.

However, some of those same analysts recently had a change of heart and adjusted their predictions. After evaluating the most recent commercial real estate trends and the rate of recovery for the economy, analysts from Morgan Stanley recently asserted that the widely expected downfall of the commercial real estate market may not come to pass. Instead, real estate investors and those holding real estate focused funds may actually see significant gains by next year – not just in years to come.

The pandemic was a tremendous burden for many in commercial real estate. The seeming 2020 dip made many commercial real estate values drop, especially in cities like New York that had so many shutdowns. But the values did not drop as some had thought they would. According to the October 2020 RCA CPPI: U.S. summary report, which The RCA Commercial Property Price (RCA CPPI) assembles as an index from a suite of price indices developed and published by Real Capital Analytics, U.S. commercial real estate prices actually rose in aggregate at a 1.4% annual rate from September 2019 to 2020, a noticeable slowdown from the mid-single-digit growth rate in 2018 and 2019.

Though prices on apartments and industrial properties actually rose (up 6.7% and 7.4% year over year, respectively), properties in the retail and office building sectors saw prices drop (5.3% and 1.5%). Depending on how long the pandemic stretches out, those prices in weaker sectors could fall even further. But, commercial real estate as a whole, especially warehousing and retail spaces, seem to be faring better than many would have projected as the world emerges from the pandemic.

Like most every other investor we work with that manages multiple commercial holdings, we expect continued strong performance and we anticipate strong gains in 2021. Most commercial real estate investors see tremendous opportunity in the recovering economy. As is the case with many other industries that have sagged during the pandemic, now we see money waiting on the sidelines and opportunities for investments. Many real estate funds have been greatly influenced by the thriving performance of the U.S. stock market and the potential of money flowing back into commercial real estate and related funds (especially with treasuries and other bond yields remaining so low), the market is likely to recover - and gain momentum - quicker than anyone thought just two quarters ago.

According to RCA, U.S. commercial real estate activity rose in March compared to a year ago, with deal volume increases seen for most of the major property sectors, the latest edition of US Capital Trends shows. For the first quarter in total, deal activity dropped by nearly 30% compared to Q1 2020.

March deal volume increased 11% versus March 2020 when the pandemic first erupted and cracks started to show in U.S. deal activity. Sales of office, industrial and apartment properties all grew. Deal activity in the hotel sector spiked higher, though this was due to one large portfolio of nearly 200 properties.

The industrial sector continues to shine. Sales of individual properties reached $14.4 billion in Q1 2021, a record high level for a first quarter. Construction of industrial properties expanded in the majority of top U.S. markets during the past four quarters, with Dallas at the forefront. Industrial construction starts increased 67% year-over-year in Dallas, and it was also the leading market for apartment construction during the COVID era so far, U.S. Capital Trends shows.

To summarize, while some have said it will take years for cities – and commercial real estate within cities – to recover from the pandemic, the hard data tells a different story.

Vladislav Poshmorga is general partner at REDV, a commercial real estate development fund, Claymont, DE