



The strength of the US dollar will help maintain a robust commercial real estate capital market - by Michael Zysman

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As the US economy is arguably in a recession and the Federal Reserve's policy in the near term is to continue forward with Quantitative Easing or QT, the strength of the US dollar should help

maintain a relatively strong commercial real estate debt capital market for prime assets and prime sponsors. Over the past 12 months the US dollar has outperformed the US and international stock markets, publicly traded real estate indexes, long duration bonds indexes, almost all major currencies, and other assets that are deemed benchmarks of stability. One of the main creators of value for the commercial real estate industry is the availability for debt capital. Due to the dollar's strong performance over the past 12 months and the recent increase in interest rates, capital from both the US and around the world are actively investing in US bonds, CD's and mortgages which add considerable liquidity to the commercial real estate debt markets. The recent decreases in long-term interest rates for commercial real estate is most likely due to this increased demand from private investors.

For the 12-month period ending August 9, 2022 when compared to the US dollar, the British Pound is down 12.8%, the Euro is down 13.2%, the Yen is down 18.7%, the Rupee is down 6.9%, the MSCI US REIT index is down 5.7%, the S&P 500 is down 7.7% and the Nasdaq 100 is down 13.6%. As interest rates increase, investing in US denominated debt instruments such as commercial mortgages with strong underwriting standards becomes a very attractive investment. Not only would an international investor receive interest payments on their investment, they would also receive an increase in value if the US dollar continues to strengthen vs. their home currency. This can result in substantial risk adjusted returns. In addition, the increase in value of the US dollar has also been an inflation hedge for foreign investors.

The attractiveness of the US dollar when compared to these other currencies is due to the relative strength of the US's economy, military, checks and balances of the legal and political system, size of its consumer market, its natural resources, production of advanced technologies, advanced healthcare technology, its higher education, and its peace treaties around the world. In addition, US investments in well underwritten commercial real estate debt can create a store of safety due to a foreign investor's relative sense of instability in their home country.

The US dollar's value increases relative to demand. US dollars are needed to buy goods and services, pay interest on US dollar denominated debt, pay US taxes, and invest in US based assets. As interest rates increase, US taxes increase, inflation continues, and the bottoming out of financial markets are on the horizon, we should see an increase in demand and value of the US dollar. Also, the Federal Reserve's Reverse Repo Line which allows banks to deposit their money risk free at a set interest rate has a record balance of \$2.23 trillion which is up from a balance of \$24 million as of February 17, 2021. By paying attractive risk-adjusted short-term rates on the Reverse Repo Line, the supply of dollars decreases, which increases the relative value of the dollar when applying elementary macroeconomic principals.

The US dollar's value could have downward pressure from increased supply if the US misallocates financial resources and money in the Reverse Repo Line is quickly deployed into the capital markets. Demand can decrease if interest rates decrease, taxes decrease, inflation decreases, and if there are more attractive places for investors to deploy their capital elsewhere. By playing close attention to these factors and assuming no government intervention in the commercial real estate capital markets, we can use them as a barometer to predict the availability of debt capital in our

industry.

As investors continue to invest their capital in commercial real estate debt, it should continue to allow for healthy interest rates within our industry. As the demand for debt investment increases and investors have a hard time obtaining well underwritten loans with attractive rates, they will reallocate their capital to equity investments. This should increase real estate values over the long run and help maintain a healthy private commercial real estate capital market.

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