MSCI

May 2022

Capital Trends

US Big Picture

18.6% YOY price change

$45.0b Transaction volume

3% YOY volume change

The pace of growth for U.S. commercial property sales continued to taper in May, dropping to 3% from the double-digit growth recorded during what was a record-breaking first quarter.

Inflationary pressures and rising interest rates have thwarted deals that no longer qualify as economical. Sellers have not been quick to adjust to a rapidly changing environment, exacerbating the price expectations gap between themselves and potential buyers, and leading to a more moderate pace of deal flow.

Given current economic conditions, investors and lenders are finding it necessary to reassess pricing in real time. A look at average commercial and multifamily LTVs suggest that lenders are not able to support valuations from earlier in the year. In April, commercial LTVs averaged 56.7%, down nearly 50 bps from March. For multifamily mortgages, LTVs averaged 60.5%, down over 100 bps. With lower leverage and rising interest rates, buyers must reevaluate if return targets can be reached at current prices.

Still, the market remains liquid. Even at this muted pace of deal growth, volume for the month was 5% higher than the average May during the five years prior to the pandemic. Single asset sales did decline 4% on an annual basis, but the level in May was 14% higher than the average pre-pandemic May.

Across the core property sectors, only apartment, retail, and hotel properties posted positive growth in deal volume versus the prior May. For the retail and hotel sectors, activity for the month was grounded in single asset sales, with megadeal activity accounting for less than 20% of volume in either sector.

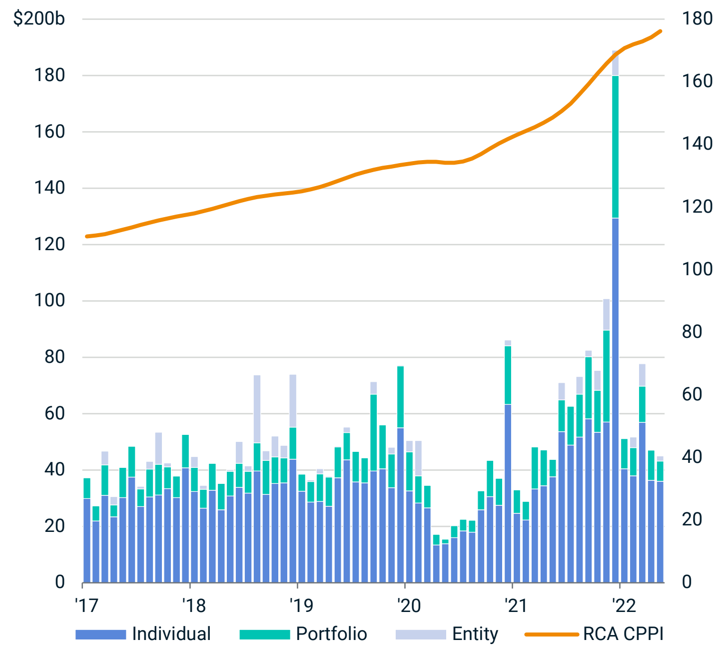
Transactions do not happen overnight and thus it can be expected that prices will not recalibrate immediately. In May, the RCA CPPI All-Property Index climbed 18.6% YOY. Still, price growth has been decelerating since January when growth had reached 19.3%.

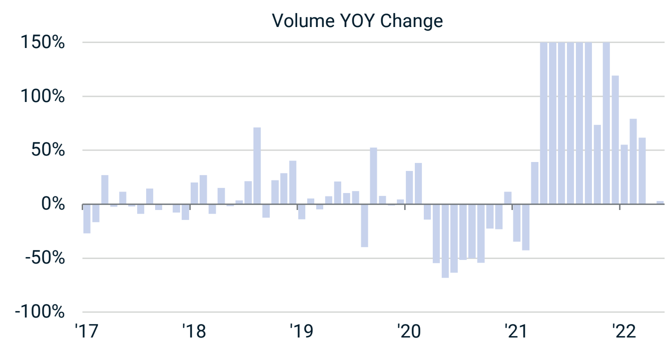
Transaction Volume Summary

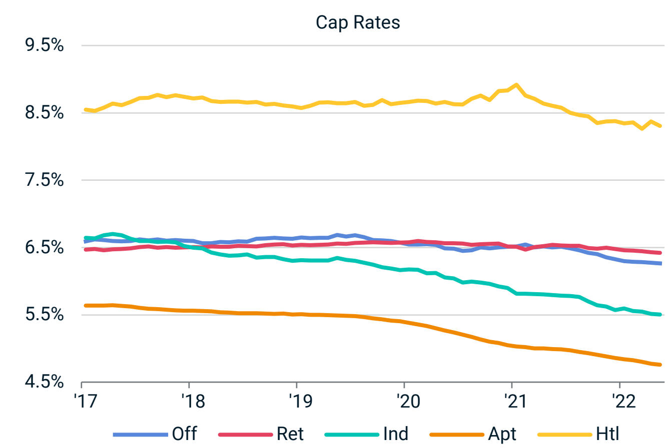
	May 2022		YTD 2022			RCA CPPI
	Vol ($b)	YOY	Vol ($b)	YOY	Cap Rate	YOY
Office	5.1	-34%	47.2	24%	6.3%	12.2%
Retail	5.9	34%	31.7	73%	6.4%	18.8%
Industrial	7.2	-20%	52.0	21%	5.5%	28.6%
Hotel	3.1	36%	17.4	59%	8.3%	16.1%
Apartment	21.5	22%	108.7	46%	4.8%	23.3%
Snr Hsg & Care	0.8	-15%	4.1	-39%	5.9%	
Dev Site	1.5	-19%	11.5	28%		
Total	45.0	3%	272.5	36%		18.6% *

*All-Property Index comprises office, industrial, retail and apartment

Monthly Transaction Volume and Pricing







Trailing 12-mth cap rates; volume YOY change truncated at 150%

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Market Momentum in 2022

Not all buyers have been spooked by rising interest rates. Looking at the unique count of investors in the market can be useful on its own, but it stands to reason that this count will fluctuate with the number of transactions. Examining the unique count of investors as a ratio set to the count of transactions sheds light on the concentration of buyers in the market.

In Q1'22, to the extent that an investor was active, an active investor participated in more deals than they had in prior years. Compared to the average between 2015 and 2019, Q1'22 saw 6% fewer investors. At the same time, the number of transactions grew 2% versus the pre-pandemic average.

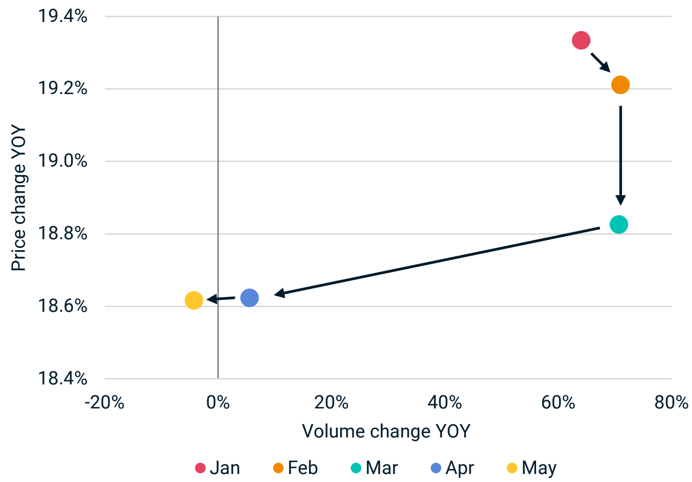
The current market conditions may be advantageous for some investors as competition within some asset classes has declined. While the total count of buyers has remained flat on a year-over-year basis, the institutional and REIT buyer classes have seen a greater number of investors transact. Those buyers with access to capital and to cheaper debt have the advantage in the current climate.

Still, no investor wants to buy at the top of the market. Despite slightly decelerating price growth, the growth in deal volume continued to contract in Q2'22. The squeeze on volume suggests that double-digit price growth set against rising interest rates and a potential demand shock has widened the gap between buyers and sellers.

Deal volume can sometimes cloud the true picture of market health. Despite record-breaking volume through May, activity as measured by the count of transactions has fallen. Through week 17 of 2022, the count of deals had been at a record level. However, by week 18, that was no longer the case.

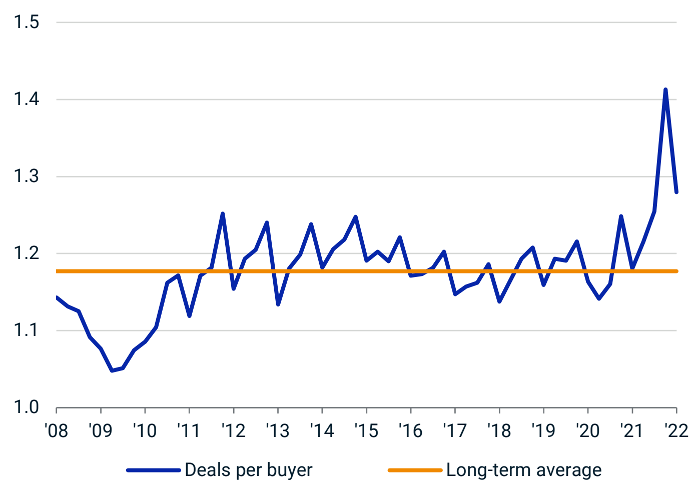
Uncertainty did not seem to impact all deal flow with the same force. Those deals at the larger end of the size spectrum — transactions priced over $50m — continued to close at a record clip. The same can't be said for those at the smaller end.

Annual Growth in RCA CPPI and Single Asset Volume

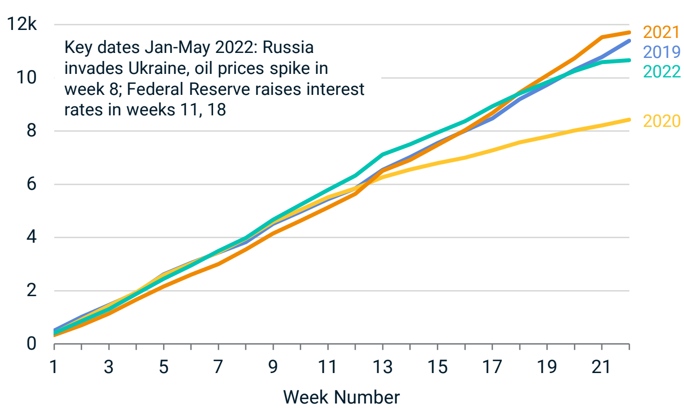


RCA CPPI National All-Property Index (office, industrial, retail, apartment); single asset volume includes all major property types

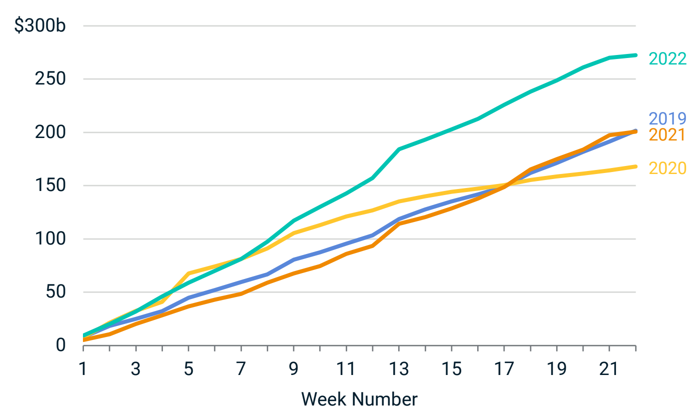
Acquisitions per Unique Buyer



Cumulative Weekly Deal Count



Cumulative Weekly Deal Volume



Spotlight on Student Housing

On the heels of a record-breaking year for investment activity, the student housing sector continued to grow in the first quarter of 2022 and cap rates remained at record lows. Deal volume totaled $2.4b in Q1'22, up 121% compared to the same period a year ago.

Sales growth at the start of the year was bolstered by sales of individual assets – the bedrock of the market. The $1.8b in single asset trades was a record-high level for any first quarter and accounted for more than 75% of total sales volume. Portfolio sales activity more than doubled from a year ago to total $545m.

Student housing cap rates, as measured by the RCA Hedonic Series (RCA HS), were at 5.1% in Q1 2022. (This cap rate series controls for quality and locational differences in the underlying sample.) The 5.1% figure is the same level as seen a year ago and still the lowest level the sector has shown. While student housing cap rates were static, the spread to comparable multifamily assets was not.

Most student housing properties are located on the outskirts of large universities, which are often situated outside of the major metros. The RCA HS cap rates for multifamily assets found in these non-major locales fell 40 bps from a year earlier and reached a record low of 4.5% in Q1'22. The spread between this series and student housing cap rates started to expand back in Q2'21 and now stands at 65 bps.

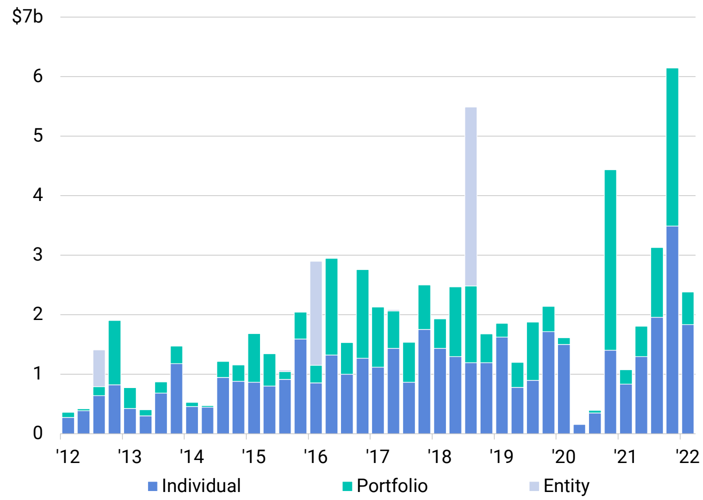
For the first five months of 2022, private capital sources were the largest source of capital for student housing properties. Their 62% market share was up from the average share of 47% they held in the same period for the years 2017-19, before the pandemic struck. Institutional/fund investors were the second largest class of investors year to date, capturing 28% of the market, up from the 20% average share they held in the first five months of 2017-19.

Blackstone is one of the leading buyers of student housing properties so far this year. While four other private and institutional players outpaced their acquisition activity through the end of May, Blackstone has more in the pipeline. BREIT, Blackstone's non-traded REIT, and other Blackstone funds plan to acquire American Campus Communities in a multibillion-dollar deal which is slated to close in the third quarter of 2022.

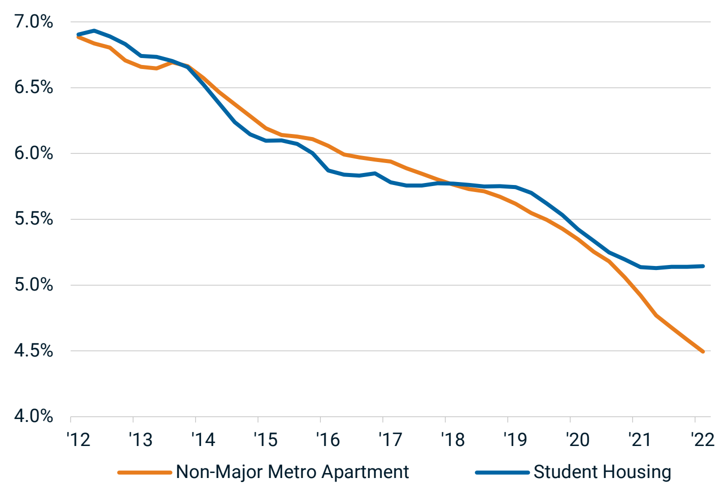
The momentum of construction starts in the student housing sector has not mirrored that of acquisition activity. In the four quarters through Q1'22, starts totaled 12,500 units, down 5% YOY. This is the seventh consecutive quarter, on a four-quarter trailing basis, that the sector has registered declines in construction starts. Despite increased demand for student housing, developers appear to be showing restraint.

As cap rates of traditional multifamily assets push to new record lows, the relative yield opportunity offered by student housing may further pique investor interest.

Quarterly Deal Volume

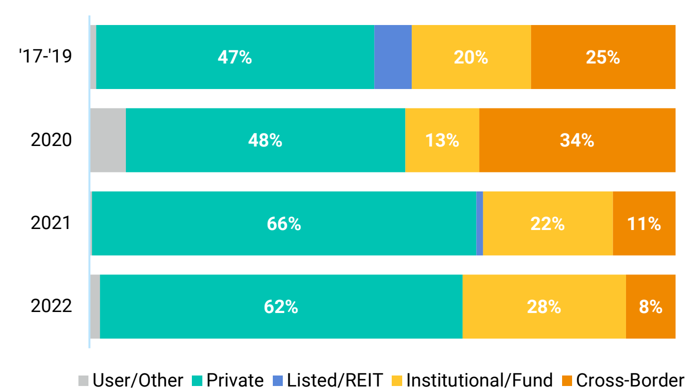


Cap Rates



RCA Hedonic Series

Investor Composition



January through May for each period

Cross-Border Investment in the US

Cross-border investors were net sellers of U.S. commercial real estate in aggregate in the first quarter of 2022 and across all the major property types were net buyers of only industrial assets.

After a strong end to 2021, when cross-border volume represented 10% of total U.S. property acquisitions on a pure quarterly basis, the cross-border share in the first quarter of 2022 dipped to 5%. For the past four quarters on average, the share was 8%.

The industrial sector garnered 35% of spending by cross-border investors in Q1'22, the highest share for this property type on record. Still, the net quarterly acquisition volume of $1.6b was low relative to the total for 2021, when overseas investors added $15.3b of industrial assets.

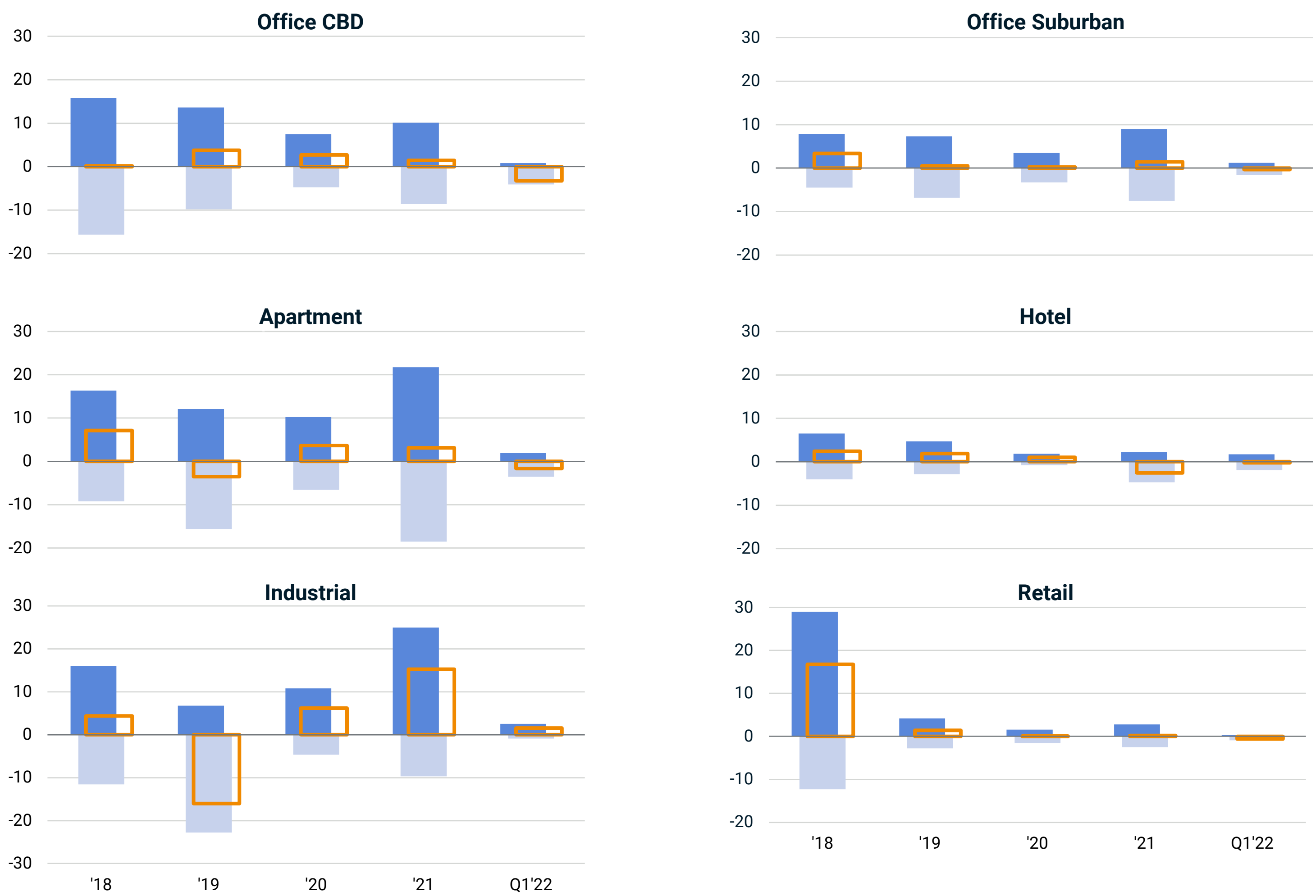
Cross-border firms were net sellers of office assets in Q1'22, primarily due to the selling of CBD office assets. Cross-border acquisitions of CBD office assets in the first quarter were 79% below the pre-pandemic average (2015-19) for a first quarter, while cross-border dispositions of such assets were 86% higher than the pre-pandemic average.

Hotel purchases by cross-border investors totaled $1.7 billion in the first quarter of 2022, representing more than 75% of the cross-border acquisition total in this sector for the whole of 2021. Still, these investors remained net sellers of the hotel sector for a fourth consecutive quarter as they disposed of $1.9b of assets.

Canadian and Asian investors led the rebound in cross-border activity in 2021 but slowed down in Q1'22. Acquisitions by firms headquartered in Canada fell 24% YOY and for Asia-based investors the drop was 8%. Canada remained the number one source of capital into the U.S. for the past four quarters, followed by Singapore and South Korea. Germany and Bahrain rounded out the top five sources.

The Q1 2022 US Cross-Border Investment Compendium data file is available for download from the client website.

Net Investment by Property Type



$ billion; data at June 2

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Chief Economist, Real Estate Research

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Vice President, Real Estate Research

Wyatt Avery
Senior Associate, Real Estate Research

Michael Savino
Senior Associate, Real Estate Research

Cole Barker
Analyst, Real Estate Research

Methodology

Data based on properties and portfolios $2.5m and greater unless otherwise stated. Data as of June 21, 2022 unless otherwise stated.

About Capital Trends

Capital Trends reports analyze and interpret trends in the global real estate market. US Capital Trends is a monthly edition comprising an overview of the U.S. market and separate reports on the five main property types. Asia Pacific, Australia, Europe and Global Capital Trends are published quarterly.

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