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# An appraiser's look at 2012: Low mortgage interest rates expected to remain during 2012

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Demand for commercial real estate property is largely a function of general economic activity. At present the U.S. economy is perceived as being relatively weak despite recent improvements. However, business is starting to reinvest and consumer spending is increasing. The consensus is for relatively modest national economic growth, perhaps 2% in real annual GDP during 2012 through 2013.

Connecticut's State Gross Domestic Product grew about 3% in 2010, and is expected to have grown about 3.5% during 2011. Employment gains have been modest; only 29% of Connecticut jobs lost from the peak have been retained.

Investment demand and price trends vary by sector. Apartment building fundamentals have been helped by strong tenant demand. Mortgages are available at favorable terms and capitalization rates have declined over the past two years. Strong investor interest has lead to a seller's market. Well-tenanted apartments in good locations are especially attractive and per dwelling sale prices approach price ranges observed in 2006 and 2007. In contrast certain older apartment properties with poor occupancy are distressed assets which are trading at relatively low price levels.

In the industrial sector there is strong owner-occupant demand for modern good quality industrial buildings in the 10,000 s/f to 45,000 or 60,000 s/f range. Prices are down from year 2007 peaks, but low interest rates enable buyers to pay relatively good prices for modest sized buildings. In contrast there is an over-supply of industrial buildings containing more than 100,000 s/f and per unit sale prices and lease rates have fallen substantially for this product type.

Retail markets have been hurt by the post financial crisis decline in disposable income which resulted in weak demand for retail space. While holiday 2011 sales were up, changes in retail behavior are causing disruptions. As online sales become more important, demand for physical stores is reduced. Some retail organizations are creating a small number of large stores for showcase purposes, complemented by smaller concept stores. Larger companies with multiple outlets have competitive advantages with respect to cost, access to capital and supply chain efficiencies. The smallest retailers have largely lost the ability to use home equity lines to support independent stores. It is more difficult for new independent retailers to become established and small stores tend to remain vacant for longer periods of time. Vacant stores are now found even in excellent retail locations.

Connecticut's office submarkets vary in terms of health and prospects for future prosperity.

Hartford's Class A CBD vacancy rate is about 27%; it experienced negative absorption during 2011. Negative Class A absorption is expected during 2012. Class A Hartford rental rates are clustered around $21 to $24 per s/f of a full service basis. Hartford's CBD Class B vacancy rate approaches

43% and Class B rents barely cover operating expenses. The difficulties of the Hartford market are exemplified by Northland's problems with CityPlace II and the Goodwin building. Greater Hartford's suburban office vacancy rate is just shy of 20% with weak demand primarily the result of slow job growth. The pending sale of CityPlace I, an 885,000 s/f office tower, for $99 million, or $112 per s/f, is the signature deal for the capitol city. The buyer is CommonWealth REIT of Newton, Mass.

Fairfield County benefits from its close proximity to New York City. During the fourth quarter of 2011 renewals and expansions of office space within Fairfield County were positive. The vacancy rate in Stamford's CBD is about 26%; pricing is relatively strong with Class A rents about $36 per s/f, an increase above the prior year.

The signature office deal in Fairfield County involved the year-end sale of The Financial Center, a 560,000 s/f building located at 695 East Main St., Stamford. Formerly the headquarters for General Reinsurance Corporation, the now vacant building sold for $30 million, indicating a unit price of about $54 per s/f. It was purchased by an affiliate of Building and Land Technology, a major Stamford-based developer/investor.

One positive element in the commercial real estate market is the Fed's liberal money policies. Fed actions have kept mortgage interest rates at very low levels and low rates are expected to remain during the election year of 2012. Low interest rates tend to reduce capitalization rates and thus help to increase real property values. This fosters investor demand for commercial property.

Arnold Grant, CRE, MAI is president of Arnold J. Grant Associates, Inc.. Hartford, Conn.