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Both single tenant and net leased assets and shopping center sales are up with much coming in net lease sector

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The New England offices of Marcus & Millichap (Boston/Connecticut) have seen a healthy amount of activity in the retail markets over the past year. The net lease sector is absolutely on fire. Both single tenant net leased assets and shopping center sales are up over last year with much of that activity coming from the net lease sector.

The primary drivers continue to be aligned with recent trends, including massive over supply of both investors and capital targeting the Northeastern markets especially New England's anchor, Boston. An incredibly favorable low interest rate environment and the barren landscape for new development in the retail sector have impacted current activity levels. There is also a consistent pattern of long term investors remaining on the sidelines not quite ready to make a move in the market. These factors combined create a perfect storm in the marketplace. The excess supply of both qualified investors and availability of inexpensive capital are pushing up against a diminished supply of inventory to drive cap rates to an all time low, surpassing even the last significant upswing in values with no definitive end in sight.

An emerging trend is the increased level of activity in the secondary and tertiary markets which offer better yields to investors under identical credit scenarios. The uptick in retail strip center activity, especially when leased to national credit tenants, comes from how closely they mimic single tenant net leased properties while offering comparatively higher yields. Given the limited construction taking place, new projects are being developed in fairly conservative terms and are largely delivered pre leased thereby reducing the impact to overall market vacancy.

The moderate retailer expansions throughout the market, predominantly in the discount retail segment, also contributed to the overall vacancy factor (50 basis point decrease over previous year). While improving employment figures are leading to greater opportunity for expansion and increased construction they are primarily focused in core urban markets.

The New England markets are performing well, in general. With employment growth in the higher paying technology, life sciences and financial services sectors there is new household formation. This is a correlation to the boom in development in Boston and surrounding area which is driven primarily by new young professionals seeking a more urban living environment. Overall unemployment continues to gain traction reaching a five year low in 2014 and surpassing the prior 2007 peak for unemployment while consumer spending has been very resilient despite higher taxes and weather related incidents typically associated with weaker spending. U.S. household wealth reached \$81.8 trillion earlier this year spurred by recovering equity markets, rising home prices and lower levels of mortgage debt. Further evidence from rising import figures points to greater underlying strength in domestic consumer spending for 2014 and beyond.

Near term expectations include continued deal velocity in the net lease space and an uptick when

combined with the increasing construction throughout the market. Much of this volume will continue to be driven by cap rate compression and low interest rates. Inventory will come from developers that held projects built in the last construction boom, investors wishing to capitalize on market compressions for a significant gain on stable assets and second or third generation value add opportunities. While trends are positive there remains concern over the implications of shorter term low interest debt when considering the likely increase in interest rates in the coming years. If job growth can continue at nearly 230,000 positions per month as averaged this year, it will go a long way in supporting the housing recovery which will further drive retail sales. While slightly down from last year, current figures for single family home sales remain near the long term annualized trend of approximately 4.4 million units. The increasing inventory of homes plays some role in this equation but also demonstrates the improving confidence in the market and should ultimately help drive sales volume up.

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