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Growth and underwriting: Keep your hands on the wheel - by David Kirk

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Commercial real estate investment benefits generally from economic growth. Slicing and dicing the data and going deeper than the headlines and sound bites provides greater comfort for the commercial property investor. Deals are underwritten on the ground versus commercial airline altitude. Still, the good news is Gross Domestic Product (GDP) increased at an annual rate of 3.2% during the first quarter of 2019 versus 2.2% in the last quarter of 2018. The advance estimate by the U.S. Commerce Department Bureau of Economic Analysis (BEA) was embargoed until its release April 26. The Massachusetts economy outpaced the nation at 4.6% for the first quarter 2019. MassBenchmarks, published by the University of Massachusetts Donahue Institute in cooperation with Federal Bank of Boston, reported April 26, that fourth quarter 2018 gross domestic product estimate for Massachusetts was 2.3% based on current data versus national fourth quarter 2018 of 2.2%. Good macro makes good commercial real estate.

Underwriting is driven by micro economic diligence and anecdotal data. And supported by macro-economic trends, current and forecast. Positive resonance at the macro level can qualify the availability of capital and terms and conditions. Local trends are generally more difficult to refine for singular relevance for any investment. That said, the upward recent economic growth reported in the nation and Massachusetts is good news for fundamentals. Demand derived from the constituent wellbeing measured by employment and wages and corporate profit drives property performance. Rents and occupancy that determine investment benefits are pressed upward in periods of expansion, increased economic growth.

Every line on the commercial real estate pro-forma is a derivative of local economic trends and dependent on primary research. Headwinds or tailwinds are discernible. The positive trends in employment and wages trickle into and impact costs for services, payroll and utilities at the property level, enough to lift and dampen prospects for property investment and performance.

Economic growth is just a snapshot of complex aggregations of a variety of revenue source data and related projections. Growth algorithms for processing economic data are challenged by sectoral changes in technology and demographics and globalization. Rethinking methodologies of what and how to count are continuously propelling growth and obsolescence of base line data. Nothing new. Velocity of these changes might well have increased based on related academic commentary. Job activity clearly supports upward growth data. And commercial real estate property performance confirms the positive economic activity. So peripheral activity reports and vision are good. Keep your hands on the wheel!

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