Interest rates and inflation - by Matthew Bacon

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As we all know, interest rates have been changing drastically, with movement in both directions, depending on the type and term of financing. The Federal Open Market Committee has taken drastic action in efforts to curb abnormally high inflation, but it hasn't controlled labor cost growth to the extent that was intended. In the northeast, and New Hampshire in particular, housing costs, labor costs, and many other indicating products and services have spiked dramatically.

Looking forward, most experts expect the Fed to continue raising rates to a peak of 5% or more, and then holding steady. What does that mean for us and CRE in particular? That's where the rate outlook becomes more unclear, as it's not a 1:1 correlation to the Fed target funds rate.

In an article published by JPMorgan Chase in December 2022, Mike Kraft, commercial real estate treasurer for commercial banking at JPMorgan Chase was quoted as saying, "The Fed's actions on short-term rates don't directly translate to a like effect on fixed rates underlying commercial real estate mortgages. After any Fed rate hike, it's possible that fixed rates might rise or fall depending on circumstances." This has certainly been illustrated by movement in both directions in the 4th quarter of 2022, despite unidirectional movement to the target federal funds rate.

In a recent discussion with Michael Chase, CCIM, managing director of debt and equity for NorthMarq in Boston, he explained some historical movement reinforcing Kraft's sentiment. "Interest rates have been on a decline since early November following a series of economic indicators showing inflation appears to be on a downward trend. While borrowing conditions have improved for long-term fixed-rate financing, those seeking short-term and floating-rate debt are still facing elevated interest rates." As rates in the commercial finance sector have not spiked as sharply as residential and consumer borrowing rates, the impact to CRE valuation hasn't been nearly as drastic in New Hampshire.

Chase continued, "Elevated floating rates may start to stress borrowers with existing loans unable to cover debt service or those that have upcoming loan maturities. This may lead to some distressed opportunities. On a positive note, short-term loans backed by SWAPS appear to be making a comeback with some construction borrowers able to lock in forward rates in the 5%'s and below the floating interest rate they may be paying during construction."

As we look forward to the 2nd quarter of 2023, several large local developers continue permitting activities and filings for anticipated starts later this year and early in 2024, indicating some resilience in new starts. Meanwhile, NECPE statistics show 37 properties sold and leased in the first three weeks of 2023, out of which only three were land, showing good activity in existing product.

Member motivation for February - statewide involvement - our NHCIBOR BoD and committees always welcome interested parties to get involved in one of our committees, but this month, I would like to put a call out for involvement at the state level. NHAR could use your insight and support on committees such as the Public Policy Committee, Communication Committee, and more. It's very important that the commercial practitioners continue to have a voice at the state level, so please consider serving on one of NHAR’s committees this year or next!

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