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## **Commercial markets observations: Making sense of the various sectors is a challenge - by Bill Pastuszek Jr.**

September 06, 2024 - Northern New England



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Let's take the Red Sox. Last year, they were last in the division with 78 wins and a .481 percentage. This year, to date, they are third in the AL East with 66 wins and a .528 percentage with a chance for a wild card. That's progress - if they keep it up.

Looking at commercial markets, is there some similar improvement seen? Are there glimmers of hope of some property sector going on a hitting streak?

More than halfway through the year, commercial markets continue to deal with high mortgage rates, higher cap rates, compromised properties, lower values and an unsatisfying amount of transaction data. Making sense of the various sectors is a challenge, given that they do not move in unison and are affected by different influences. One survey considers market conditions in the first half of 2024 representative of a "fluid situation."

A survey that analyzes repeat sales activity notes that general commercial markets have performed more strongly than investment grade markets. The index showed a steep drop at the end of 2022 into 2023 with the last several months showing some recovery.

Negative absorption is noted for several quarters in office, retail, and industrial sectors. Rent growth in apartment rents in Boston was +2.8%. Boston is in the 25% of markets surveyed.

Interestingly, Boston ranks high in multi-family, retail, and office markets.

Cap Rates. Cap rates for most income property types are prime indicators of market direction. However, in order to make valid comparisons, it is necessary to understand how cap rates are developed from various sources so that adjustments can be made if necessary to allow for apple-to-apple comparisons. Without a consistent basis, an analyst risks misinterpreting the market.

There seems to be some consensus that cap rates in most sectors have probably peaked. An exception is the office sector and there is some concern in the lodging sectors. With recent economic news suggesting there is a rationale for a rate decrease by the Fed, a lower cost of money can only have a favorable effect on cap rates. On the other hand, the uncertainty factor may have a cancelling or muting effect on overall rates.

One survey notes that the spread of rate ranges by respondents is wide. In more active markets, surveys showed that cap rate spreads among property classes tended to be tighter. Here the wide gap illustrates that respondents are providing a wide range to indicate greater uncertainty and less confidence in direction of market sectors.

Sorting out cap rates based on sales is a challenge in this market. It can be argued that a lot of properties aren't coming to market for various reasons that are somewhat opposed to each other. One source claims that "good" property owners that can are holding out for more favorable market conditions. The properties that come to market are ones where owners need to sell. There's no

consensus. It does seem that the rate environment couple with low, not necessarily representative sales activity provides a challenge to anyone trying to make sense of the market.

Conclusion. It can be said that analysts of market behavior are only as good as the data out there. But, the data is telling us something: it's our job to figure out what that is. Let's hope for less "fluid conditions" going forward. On the other hand, we should be able to rely on training and experience to make sense of the market and not just do enough to look awake.

And I don't see a commercial real estate hitting streak happening. Go Sox!

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